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The Many Fallacies of CSR

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ABSTRACT

Corporate philanthropy has always been a part of India's business culture but what had remained voluntary so far was officially inserted into the legislation governing companies with the new Companies Act 2013. In fact India became the first country to actually do something that several countries had only been discussing for years. However, unlike other countries which envisage internal tweaks in operations, India's approach to CSR is towards external philanthropic initiatives to be taken up by companies. Ever since its implementation, a lot of eligible Indian companies have gotten themselves involved in and lent a helping hand towards making India a better society. Several studies/reports have also indicated that companies too benefit from indulging in such initiatives in the form of an improved brand image, consumer loyalty as well as a motivated workforce. On the flip side, its an increased cost to the companies who could've used the money in strengthening their balance sheets or bettering their offerings.

The current CSR legislation is a great initiative but is highly flawed in its approach with its actual contribution to the development of the society being questionable. However, with some tweaks it can yield better results and truly serve as an example for the rest of the world to follow.

This article seeks to identify the numerous flaws in the legislation which enables loopholes for eligible companies to actually not contribute to the objectives envisaged by the legislation, with the backdrop of approaches adopted in other countries. It also looks at the advantages and disadvantages of having a mandatory approach towards Corporate Social Responsibilities and how it has fared thus far. Lastly, the paper offers solutions to the problems faced by the legislation in achieving its desired objective as well as suggestions for strengthening the legislation even further.

I. INTRODUCTION

Corporate Social Responsibility ("CSR") refers to companies adopting a business model wherein they integrate responsibility and accountability towards society into their functioning. It is wrongly believed that CSR is a western concept adopted by India. It has in fact been a part of the country's culture since time immemorial, be it in the form of the donations given by

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wealthy merchants and traders to establish religious institutions to philanthropic initiatives of wealthy business families like the Tatas, Modis, etc. While these charitable works have largely been voluntary, in 2013, India became the first country in the World to incorporate mandatory CSR into the Companies Act, 2013 ("**the Act**").[2]

CSR has been defined under the Companies, (Corporate Social Responsibility Policy) Rules, 2014[3] ("CSR rules") to mean projects or programs to be undertaken by a company in areas specified in Schedule VII or in the company's CSR policy subject to inclusion of areas specified in Schedule VII of the Act. This schedule contains a non-exhaustive list of activities, such as eradication of poverty/hunger, promotion of education, rural development projects etc., aimed for welfare of the society. A perusal of the provisions of the Act makes it clear that CSR in India refers to external initiatives by companies for social and economic welfare of the country. While CSR in India is limited to external initiatives, the concept is more comprehensive elsewhere. For instance the definition of CSR as set forth by the United Nations Industrial Development Organization includes integration of social and environmental concerns in business "operations and interactions with their stakeholders".[4] Likewise, the definition enumerated by the European Commission i.e. the executive branch of the European Union, lays emphasis on integration of these concerns into the "business strategy and operations"[5] while the alternate term used by the OECD called "Responsible business conduct" also lays down non-binding (on members) guidelines for companies ranging from contribution for economic and social development to recognition of human rights in their conduct.[6] India already has laws in place for strategic and operational matters within a company hence the scope of this paper will be limited to CSR as set forth in Section 135 of the Act, The Companies (Corporate Social Responsibility Policy) Rules, 2014 and the changes contemplated by the legislature in the form of proposed amendments.

CSR benefits the society as a whole by supplementing government efforts in trying to uplift the economic and socially depraved sections of the country. The companies in turn benefit from

[2] Indo-Asian News Service, *India Now Only Country with Legislated CSR*, Business Standard (April 3, 2014, 17:51 IST), https://www.business-standard.com/article/companies/india-now-only-country-with-legislated-csr-114040300862_1.html

[3] Companies (Corporate Social Responsibility Policy) Rules, 2014, Gazette of India, pt. II sec. 3(i), https://www.mca.gov.in/Ministry/pdf/CompaniesActNotification2_2014.pdf (February 28, 2014)

[4] UNIDO, What Is CSR?, https://www.unido.org/our-focus/advancing-economic-competitiveness/competitive-trade-capacities-and-corporate-responsibility/corporate-social-responsibility-market-integration/what-csr (last visited November 8, 2019)

[5] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of Regions: A renewed EU strategy 2011-14 for Corporate Social Responsibility, COM (2011) 681 final (October 25, 2011)

[6] Org. for Econ. Co-operation and Dev. [OECD], OECD Guidelines for Multinational Enterprises, (September 29, 2011), https://doi.org/10.1787/9789264115415-en

a positive reputation, increased morale of the employees from the feel-good factor of doing charity and better consumer loyalty. In a way, when companies spend money to educate, nourish and uplift the weaker sections, they are doing those things to their own potential future customers and investors. CSR can also act as a measure of appeasement to the critics of capitalism. On the downside, it is an added cost to Indian companies which in turn leads to an increased cost of production and prices of goods and services which has to be burdened by the very consumers who they might be trying to uplift. The mandatory nature of CSR for Indian companies also makes them less competitive in the global market as this is one cost the companies cannot cut down. Increased workload on the existing employees or the cost of hiring additional employees is yet another drawback.

CSR can be a game changer in how companies work globally and can bring in innumerable benefits to the society as well as the companies themselves. However, the mandatory nature of CSR, as is the case in India, is something that needs a lot of deliberation. This paper tries to find out how CSR has evolved since the Companies Act and whether or not it has been a success.

II. Loopholes under the present regime

As mentioned above, CSR is not defined under the Act but und under the CSR rules. The definition itself is a bit arbitrary as even though it is defined as ‘projects or preprogrammes relating to activities specified in Schedule VII’, the definition starts with the words ‘CSR means and includes but is not limited to’. In fact the words ‘cover subjects enumerated’ in Schedule VII were changed to ‘include activities, areas or subjects specified’ in Schedule VII in a CSR policy by a 2018 amendment to the rules.[7] It can be inferred that the definition of CSR, as defined in the CSR Rules, is not exhaustive and the activities mentioned in Schedule VII are just examples of the kind of activities that the Government expects the Companies to take up i.e. Schedule VII is there to send the companies in the right direction. On the other hand, Section 135(3) of the Act[8] says that a CSR policy prepared by a company “*shall indicate the activities to be undertaken by the company in areas or subject, specified in Schedule VII*”, which appears to limit CSR to areas specified in Schedule VII. The idea of leaving CSR open to interpretation was to let companies get creative with the projects they undertook and take up projects that an elected government might find difficult to implement due to political reasons or otherwise. The idea was to have CSR fill in the gaps left by the government. Even though a

[7] Companies (Corporate Social Responsibility Policy) Amendment Rules, 2018, Gazette of India, pt. III sec. 3(i), Rule 2(1)(c)(i) (September 19, 2018)
[8] Companies Act, 2013, No. 18 of 2013, Acts of Parliament § 135(3) (India)

notification issued by the Ministry of Corporate affairs has clarified that Schedule VII is to be interpreted liberally[9], it is still not clear whether the companies can or cannot work in areas outside the said schedule. The changed definition laid out in the proposed Draft Companies (CSR Policy) Amendment Rules, 2020[10] ("**Proposed Rules**") does not provide clarity in this regard. According to Rule 7 of the CSR Rules, expenditure not in conformity or not pertaining to the areas specified in Schedule VII is not to be counted as CSR expenditure. This has further added to the confusion. This rule however, seems to have been omitted in the Proposed Rules, which seems to be a step in the right direction. Alas, at present, having a list of areas to be chosen from vitiates the possibility of identification of new areas and development therein. Companies are also more likely to stick to basic projects to avoid the risk of spending on something that may not even get counted.

Under Section 135 of the Act, a company having a net worth of INR 500 Crores OR a turnover of Rs. 100 Crores or more OR a net profit of Rupees 5 Crores or more during the immediately preceding financial year is required to spend at least 2% of the average net profits of the company made during the three preceding financial years on pursuance of its CSR policy.

Under Section 135(1), every eligible company is required to constitute a CSR Committee consisting of 3 or more directors with at least one of them being an independent director (companies not having an independent director can have a committee of 2 or more directors). The committee is responsible to formulate and recommend to the board, a CSR policy enumerating the projects to be undertaken and amount to be incurred thereon. It is also responsible to monitor the implementation of the CSR policy from time to time. This requirement of companies to form CSR committees can lead to an increased compliance and administrative cost for companies. It makes no sense for companies to undergo the trouble when the amount to be spent is less. Eg when a company is required to spend just INR 10 Lakhs on CSR then for the company to form a committee is just not worth it. If a company has made an average profit of INR 2 Crores, it will be required to spend 4 lacs. It is thus not worth dealing with all the compliances and costs associated with it to dispose of such small amounts. Even though companies are allowed to spend 5% of the CSR expenditure on administrative overheads associated with CSR[11], it is still a wastage of time and effort which could have been

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[9]Clarifications with regard to provisions of Corporate Social Responsibility under section 135 of the Companies Act, 2013, General Circular No. 21/2014, https://www.mca.gov.in/Ministry/pdf/General_Circular_21_2014.pdf (India)
[10] Draft Companies (CSR Policy) Amendment Rules, 2020, Rule 2(c) (uploaded on the Ministry of Corporate Affairs' website for taking feedback)
[11] Ministry OF Corporate Affairs, FAQs on CSR Cell, http://www.mca.gov.in/MinistryV2/faq+on+csr+cell.html (last visited February 6, 2020) (India)

used in achieving the profit objective. Such cases aren't necessarily outliers. In financial year 2015-2016, 846 companies spent between INR 10 Lakhs to 20 Lakhs[12]. It is not fair for companies to go through the expenses of complying with CSR norms to dispose of such small amounts. The proposed Companies (Amendment) Bill, 2020[13] ("**Proposed Bill**") provides a possible respite but letting companies required to spend less than INR 50 Lakh to do so through the board of the company, without having to form a CSR committee. It is also worth pointing out here that companies that were giving more than 2% prior to the 2013 Act have in fact now scaled back their charitable spend.[14] This could be because in the absence of a qualifying percentage of charity, companies wouldn't know how much is enough but with the 2% requirement in place there is no incentive to spend more than that.

Previously the fact that companies could just get away by specifying the reasons for not being able to spend gave the impression that CSR was in fact voluntary and only reporting was mandatory, that has however changed with the 2019 amendment which now necessitates (not yet notified)[15] the companies to send their unspent CSR amount to an account to be opened by companies for a financial year and for the policy drafted for that year in a schedule bank wherein the money is to be used within 3 years and if still unspent, it is to be contributed to the funds listed in Schedule VII. This is definitely a welcome change but the Act still encourages the companies to spend their CSR amount within a year and specify reasons for not being able to do so in the board's report. Even though the companies have the option of using the unspent amount in pursuance of their CSR policy till 3 years, there is no other option after that but to transfer the amount to one of the government funds. This rigid time limit can potentially act as a deterrent for companies to take up projects which have a longer gestation period which will essentially kill the creativity expected from companies in implementing their CSR policies. It is worth pointing out here that the Proposed Rules have a provision for multi-year projects having timelines not exceeding three years.[16] Even if imprisonment is repealed, penalty imposed for non-compliance will scare the companies into either directly contributing to the funds mentioned in Schedule VII or shy away from taking up projects with a longer gestation period. This goes against the very essence of CSR and will turn out to be nothing but just an

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[12]Ministry OF Corporate Affairs, An assessment of CSR expenditure of 5097 companies for the year 2015-16, http://www.mca.gov.in/MinistryV2/csrdatasummary.html (India)

[13] The Companies (Amendment) Bill, No. 88 of 2020, § 27 (as introduced in Lok Sabha)

[14]Oliver Balch, *Indian Law Requires Companies To Give 2% Of Profits To Charity. Is It Working?*, The Guardian (April 5, 2016, 05:00 BST), https://www.theguardian.com/sustainable-business/2016/apr/05/india-csr-law-requires-companies-profits-to-charity-is-it-working

[15]As on 01/04/2020

[16] Draft Companies (CSR Policy) Amendment Rules, 2020, Rule 2(h) (uploaded on the Ministry of Corporate Affairs' website for taking feedback)

added tax. In addition to that, it is not clear what is to happen to the interest accrued on the money kept in the bank for 3 years. Logic dictates that the interest accrued should also form part of the CSR amount deposited in the bank meaning the amount to be spent should be the original CSR amount + interest accrued. However, Section 135(6) is worded in a way that it can be inferred to mean otherwise. The said section says that 'any amount remaining unspent' is to be deposited in a separate account made for this purpose in a Scheduled Bank and 'such amount' is to be spent within 3 years, if unspent, 'the same' is to be transferred to a fund. The interest might sound like a small amount but it can be huge for some companies. Eg. Reliance Industries Limited which spent INR 745.04[17] Crores on CSR in the financial year 2017-2018 could have earned around INR 143.05 Crores as interest had it kept the money in a bank account with a simple interest rate of 6.40% per year.

First proviso to Section 135 lays down that preference shall be given to local area and areas around the place of operation of companies. This proviso has largely been criticised as companies tend to be concentrated in certain areas and certain industrialized states which already tend to have a higher degree of socio-economic development. The discrepancy is clearly evident from the fact that the states of Maharashtra, Karnataka, Andhra Pradesh, Gujarat, Tamil Nadu and Delhi have received approximately 40% of the total CSR expenditure from the year 2014-2015 to 2017-2018.[18]Maharashtra has itself spent INR 8468.28 Crores on CSR from the year 2014-2015 to 2017-2018 which is more than double that of Karnataka (the second highest spender) which spent INR 3014.57.[19]Out of the total amount of INR 13326.69 Crore spent on CSR activities, INR 7436.52 Crore was the share of local area expenditure which amounts to over 50%.[20]It is sometimes argued that this proviso lets companies wrongly believe that it is a mandatory proviso and not a recommendatory. This is however far from the truth as is evident from the fact that Maharashtra which was the place of origin of INR 18,682.56 Crore of CSR funds had INR 12,423.49 Crore going out to other states amounting to around 66% outflow. On the other hand Sikkim which has generated no CSR funds received INR 16.80 Crore from other states. The top 5 states in terms of CSR generation are all net donors while the bottom 5 are all net receivers. These numbers do not indicate the pan India projects disclosed by companies.[21]This shows that companies are aware that the proviso is not

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[17]Ministry OF Corporate Affairs, National Corporate Social Responsibility Data Portal, https://www.csr.gov.in/index_across.php (last visited March 10, 2020)

[18]Report Of The High Level Committee On Corporate Social Responsibility – 2018, Ministry of Corporate Affairs, Government of India (2019)

[19]*Id.*

[20]*Id.*

[21]*Id.*

a mandatory one and the companies are in fact spending outside their local limits. The degree of favouritism can however not be ignored but that is hardly as big an issue as it is made out to be. Companies are inherently profit-making organisations and it is only natural for them invest in CSR locally which would allow them to also indirectly reap the benefits of their initiatives. The beneficiaries of local CSR initiatives are also more likely to be important stakeholders such as families of employees, customers, suppliers of raw materials etc. In case of manufacturing or polluting industries it is desirable that they undertake local initiatives to try to offset the damage that they have on their surroundings Eg. A factory causing air pollution in Maharashtra should ideally concentrate its CSR initiatives such as planting of trees locally instead of in far of states like Sikkim or Orrisa. Companies also have to sometimes deal with locals agitating against them, CSR initiatives can help keep such disproportions at bay. Owing to all the above-mentioned benefits, a company is also more likely to take CSR more seriously. It is also to be kept in mind that in such cases it will also be easier and cheaper for companies to monitor the implementation of their CSR policies and success thereof can act as motivators. The 2019 High Committee report had criticised the proviso and had recommended 'advising companies to engage in CSR activities by balancing local area preference with national priorities', failing to see the benefits of local CSR.

Transfer to Government fund under Schedule VII makes no sense. It provides a lazy alternative to companies actually taking the initiatives. Supporters of CSR advocate that the main benefit of CSR is that companies leverage their business effectiveness and innovation to achieve social goals. Companies are thus able to fill in the gaps left by the Government and are able to more effectively reach those places. This advantage is however lost when companies have an option to just contribute to Government funds. The contribution to these funds has increased by 30% from INR 2 Crore during 2016-2017 to INR 71 Crore in 2017-2018.[22]Both 2015 and 2019 High Committee Reports had highlighted this problem and had recommended doing away with the provision except for in the case of unspent amount after the deadline to spend is over.[23] Unfortunately nothing has been done in this regard.

Likewise, Rule 4(2) of the CSR Rules provides an option for companies to undertake their CSR activities through Section 8 companies, registered trusts or registered societies established by the companies themselves or the Sate/Central Governments. Companies may also undertake their activities through other Section 8 companies, registered trusts or registered societies with

[22]KPMG International Cooperative, *India's Csr Reporting Survey 2018* (December 2018) https://assets.kpmg/content/dam/kpmg/in/pdf/2019/01/India_CSR_Reporting_Survey_2018.pdf
[23]See supra note 17

an established track record of 3 years of undertaking similar projects/programmes provided the companies have specified the programme to be undertaken and the modalities of implementing it as well as a monitoring mechanism. Even though on a much lesser note, this provision too beats the objective of having a board driven approach to CSR by providing a lazy way with a tick-box mentality while dealing with CSR. Moreover, it appears as though international organizations such as UNICEF are not eligible to assist companies implement their CSR policies even though they might have a much higher degree of expertise and a proven track record. The Proposed Rules suggest their inclusion in implementing CSR.[24] Some have even misused this provision, according to an Economic Times investigation, cheating the system by giving donations to charitable foundations that then return the monies minus a commission is not uncommon either.[25]

The only check on companies regarding their CSR compliance is disclosures to be made in the Board's Report. As per Section. 135, companies are required to disclose, in their Board's Reports, the composition of CSR committee, contents of the CSR policy formulated by the committee and in case of failure to spend the amount set aside, reasons for such failure. Companies are also required to place their CSR policies on their websites. Rule 5(2) states that companies need to institute a 'transparent monitoring mechanism' for implementation of the policies undertaken. These don't seem enough to keep an actual check on companies undertaking CSR activities. It is no wonder that the CSR provision has been misused several times. Eg. One of the areas mentioned in Schedule VII is 'Animal Welfare' which has been relied upon to build and maintain 'gaushalas' to earn goodwill of the government in power[26] similarly CSR funds were used to fund construction of Statue Of Unity (a pet project of the Gujarat government) by way of donations (Eg PSUs donated funds worth INR 146.83 Crores)[27]made to the Sardar Vallabhbhai Patel Rashtriya Ekta Trust (SVPRET). The Proposed Rules suggest that companies spending over INR 5 Crores be made to conduct impact assessment of their projects.[28] This might help in overcoming the monitoring issue but not

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[24] Draft Companies (CSR Policy) Amendment Rules, 2020, Rule 4(3) (uploaded on the Ministry of Corporate Affairs' website for taking feedback)

[25] Dinesh Narayanan, *How Indian companies are misusing public trusts to launder their CSR spending*, The Economic Times (Oct 21, 2015, 04:00 IST) https://economictimes.indiatimes.com/news/economy/finance/how-indian-companies-are-misusing-public-trusts-to-launder-their-csr-spending/articleshow/49474584.cms

[26] Rica Bhattacharyya, *Gau Seva Enters India Inc'S CSR Stable, Companies Spending Big Money On Cow Upkeep*, The Economic Times (June 14, 2017, 13:14 IST) https://economictimes.indiatimes.com/news/politics-and-nation/gau-seva-enters-india-incs-csr-stable-companies-spending-big-money-on-cow-upkeep/articleshow/59134230.cms?from=mdr

[27] Pushpa Sundar, *Social Projects Bypassed As Firms Spend CSR Funds To Curry Favour With Govt* Business Standard (December 23, 2018, 12:31 IST) https://www.business-standard.com/article/economy-policy/social-projects-bypassed-as-firms-spend-csr-funds-to-curry-favour-with-govt-118122300158_1.html

[28] Draft Companies (CSR Policy) Amendment Rules, 2020, Rule 8(3) (uploaded on the Ministry of Corporate

without adding to the costs and efforts required. The Proposed Rules further suggest allowing 10% instead of 5% of the CSR budget to be spent on administrative overheads in such cases but that doesn't reduce the effort and human resources required.[29] If companies are made to conduct these studies then they will most certainly prefer doing CSR in areas where they are based as it would be easy to monitor thus defeating the efforts of the Ministry of Corporate Affairs to bridge the geographical divide in terms of CSR expenditure.

Under the present legislation, there is no clarity on who gets ownership of assets created by companies as a part of their CSR initiatives. The Proposed Rules place the ownership with companies 'established under section 8 of the Act having charitable objects or a public authority'.[30]

It has also been clarified that expenditure on CSR does not form part of business expenditure and hence is not eligible for any tax exemption. It has also been clarified that some activities[31] enumerated in Schedule VII of the Act are already eligible for exemptions under various sections of the Income-Tax Act 1961. As a result, these activities automatically become attractive for CSR expenditure. Unless there is reasoning behind keeping it this way, uniformity of tax exemption for all the eligible CSR activities is desirable. There is also discrepancy in the applicability of GST as outsourcing of CSR activities to implementing agencies attracts the tax whereas if a memorandum of understanding is entered between the two parties, the contribution is treated as a grant and therefore outside the application of GST.[32]A perusal of Section 17(5)(h)[33] suggests that Input Tax Credit ("**ITC**") is not available for *'goods disposed of by way of gift'* distributed under a company's CSR policy which was also reiterated by Kerala AAR's order in the matter of M/S Polycab Wires Private Limited.[34] Since the said section explicitly mentions 'goods', it raises questions on whether ITC is available for services provided free of cost under CSR. The entire taxation system seems to be inconsistent with respect to the CSR law in place.

The above are just some of many ways in which the CSR legislation is flawed and the main reason for it is the fact that it is extremely difficult to define and legislate CSR due to it being

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Affairs' website for taking feedback)

[29] Draft Companies (CSR Policy) Amendment Rules, 2020, Rule 7(1) (uploaded on the Ministry of Corporate Affairs' website for taking feedback)

[30] Draft Companies (CSR Policy) Amendment Rules, 2020, Rule 7(3) (uploaded on the Ministry of Corporate Affairs' website for taking feedback)

[31]contributions to Prime Minister's Relief Fund, scientific research, rural development projects, skill development projects, agricultural extension projects, etc.

[32] See supra note 17

[33]Central Goods and Services Tax Act, No. 12 of 2017, Acts of Parliament § 175(5)(h) (India)

[34]In Re. M/s. Polycab Wires Pvt. Ltd. Advance Ruling No. KER/30/2019 (Kerala Authority for Advance Ruling, GST dept.)

too broad a concept. Eg. Article 5 of the Company Law of the People's Republic of China puts an obligation on companies to *"abide by laws and administrative regulations, observe social morality and business ethics, act in good faith, accept supervision by the government and the public, and bear social responsibilities."*[35]The lack of clarity in the legislation opened a pandora's box with several interpretations of the provision and the courts using the provision to scrutinise every action by companies including labour disputes.[36]Any attempt to define and legislate it would just take out the creativity that is seen in philanthropic initiatives that have always been a part of the Indian business environment.

III. ADVANTAGES OF CSR

Despite its flaws, CSR is not all gloomy. Charity has always been a part of the Indian business sphere as previously mentioned. CSR can be immensely advantageous if done right.

It is generally accepted that the companies that engage in CSR can benefit from positive marketing and an enhanced reputation. However, there isn't sufficient empirical evidence to support this claim owing largely to the ambiguous measurement of subjective parameters like 'Brand Value', 'Brand Loyalty'. A study conducted on how CSR affected Brand Equity of Indian firms concluded that CSR does have a positive impact on Brand Equity however it is only successful in boosting the performance in the long run.[37]Similarly another study, save at an international level this time, concluded that CSR activities have a positive influence on the brand value of companies. However it also found that CSR activities related to the governance domain had the most significant impact while the ones related to the environmental and social domains had little to no impact on the brand value of companies.[38]In the absence of strong empirical evidence, it cannot be said for certain as to whether CSR activities actually have an impact on the brand value of a company as there can be uncountable factors at play. But one thing that is for sure is that the as the World moves towards a more digital era, the availability

[35] [The Company Law Of The People's Republic Of China] (Promulgated by Standing Comm. of the Nat'l. People's Cong, December 29, 1993, revision effective March 1, 2014, art. 5

[36]Li-Wen Lin, *Mandatory Corporate Social Responsibility? Legislative Innovation and Judicial Application in China*, Am. J. Comp. L. (forthcoming March 28, 2019) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3361448

[37]Anupam Singh and Priyanka Verma, *How CSR Affects Brand Equity Of Indian Firms?*, Global Business Review, April 26, 2017 at 52 (For the purpose of this study, 20 Indian firms (both public and private) (among the BSE-500) were chosen to represent various industries viz. oil & gas, power, metals & mining, NBFCs and banking. The study found a positive indirect relationship between CSR and Brand Equity. The relationship was measured by mediation of CSR and Brand Awareness/Brand Loyalty/Brand Image/Purchase Intention.)

[38]Yan Feng, Yeujun Yoon and Yingyi He, *The Impact Of Corporate Social Responsibility On Brand Value: An Empirical Study Of Top 100 Global Brands*, International Journal of Business and Social Science, October 10, 2016, at 61 (The empirical analysis has been done by checking the correlation for the 2 variables. The CSR data was sourced from Bloomberg's ESG database while the effect on Brand Value was taken from the e brand value estimates developed by the Interbrand Group. The sample population was he top 100 companies appearing in Interbrand's "Top 100 Best Global Brands Ranking.)

of information to consumers is increasing thus resulting in an increased information symmetry, when this is coupled with an increased number of options available to consumers, the brand value is certainly bound to be impacted by CSR. Now there are other spill over benefits of an enhanced reputation too such as a better reputed business being more likely to attract investors.

A largely overlooked but possibly one of the most important advantage of CSR is the positive impact it has on community. In an increasingly capitalist yet both socially and economically unequal society like India, a positive reputation in the community is of utmost importance. A classic example of this is the Coca-Cola water struggle in the Indian state of Kerala in the early 2000s. Coca-Cola had established a factory in the village of Plachimada in Kerala. Soon after, the locals started complaining of water scarcity and water pollution while the company blamed the irregular rain for the water scarcity. This led to heavy protests and long legal battles. This along with a CSE report which claimed that their soft drinks contained unacceptable levels of pesticides tarnished the company's image in the country.[39] As a result sales dropped by 30-40% in only 2 weeks amounting to a decline of 15% in 2003 as opposed to a growth rate of 25-30% in the previous years.[40]This happened despite the company getting a clean chit of sorts form the health ministry and independent research labs.[41]To make matters worse, the company decided to counter the allegations by presenting logical arguments and trying to present their side of the story but the damage had already been done and the community had already become dead set against the company. It is also to be noted that it was the same Perumatty Grama Panchayat which had given the license to Coca-Cola to establish the factory in the first place which was later at the forefront of the protests and the legal battles against the company.[42][43] This case study highlights the importance of positive community perception. Coca-Cola has since then established an NGO which among other things works with local communities to work towards water sustainability and rain water harvesting.[44]The controversy has somewhat fizzled out of the minds of the citizens of the country but it is far from dying as is evident from the 2017 boycott by Indian traders of international fizzy drinks accusing them of depleting the country's natural resources.[45] It is thus important for any business to keep these often

[39]Cristina A. Cedillo Torres et al, *Four Case Studies On Corporate Social Responsibility: Do Conflicts Affect A Company's Corporate Social Responsibility Policy?*, Utrecht Law Review, November 2012, at 51, 55
[40]Michael Pirson & Deepak Malhotra, *Unconventional Insights for Managing Stakeholder Trust* (Harvard Business Sch. Working Paper No. 08-057, 2008), https://hbswk.hbs.edu/item/unconventional-insights-for-managing-stakeholder-trust
[41]*Id.*
[42]Hindustan Coca-Cola Beverages vs Perumatty Grama Panchayat (2005) 2 KLT (Kerala HC) 554 (India)
[43]Perumatty Grama Panchayat vs State Of Kerala (2004) 1 KLT (Kerala HC) 731 (2003) (India)
[44]Anandana, *Our Projects* https://www.anandana.org/ourprojects.html
[45]Vidhi Doshi, *Indian Traders Boycott Coca-Cola For 'Straining Water Resources'*, The Guardian (March 1, 2017, 14:57 GMT) https://www.theguardian.com/world/2017/mar/01/indian-traders-boycott-coca-cola-for-

overlooked stakeholders satisfied as the 'license to operate' is no longer given by the government alone.[46] Being proactive with CSR initiatives will help keep the community in check and prevent them from agitating and also save the company the resulting litigation costs.

An extension of the above point is that the communities businesses operate in are in fact the suppliers of resources to the same businesses. This argument stems from the economic theory of Circular Flow Model. The 'household' is the one supplying businesses with factors of production viz. land, labour, capital and entrepreneurship. Households are also the ones who eventually consume what is being offered by the companies. It is thus a no brainer that a healthy and happy 'household' will lead to better profits for the companies.

Companies often go to long lengths to increase employee enjoyment to increase the level of motivation among employees. CSR can help in achieving this as it provides an escape for employees from their routine work. CSR activities is one of the few ways in which accompany can ensure that all employees come together for a cause regardless of their level/cadre within the organization. Many employees who may not be able to engage in charitable work individually can do the same via the company's CSR.[47] A motivated workforce will obviously result, although to a much smaller level, in better work and more productivity. CSR engagement can also attract potential employees, especially for managerial roles as well as reduce employee turnover. A study did find positive correlation between 'employee engagement' and 'CSR' (r = 0.608) and between 'engaged employees and 'their willingness to participate in CSR activities' (r = 0.495).[48]

When the Covid-19 pandemic hit India along with the rest of the World, the Ministry of Corporate Affairs vide a circular dated 23/03/2020 clarified that spending of CSR funds for Covid-19 would be treated as a CSR activity.[49] With the governments of the World struggling to defeat this pandemic, the Indian government could turn to the corporate for a helping hand owing to the provision of CSR under the Act.

India has one of the lowest tax-to GDP ratio at 11.2%[50] in 2017 among countries of comparable

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straining-water-resources

[46]Purushotam Savlani, *Importance Of CSR: First Advantage Philosophy*, India CSR Network (September 6, 2017) https://indiacsr.in/importance-of-csr-first-advantage-philosophy/

[47]Shweta Bapat, *CSR - An Upcoming Driver Of Employee Engagement*, India CSR Network (April 5, 2018) https://indiacsr.in/csr-an-upcoming-driver-of-employee-engagement/

[48]Maryam Hanzala Tariq, *Effect of CSR on Employee Engagement*, 8, Indian Journal of Science and Technology, 301, 304 & 305 (2015) (Data was collected via questionnaire responded by 70 working professionals in and around Mumbai)

[49]Clarification On Spending Of CSR Funds For COVID-19, 2020, General Circular No. 10 of 2020 http://www.mca.gov.in/Ministry/pdf/Covid_23032020.pdf (India)

[50]WBG, *Tax Revenue (% Of GDP) Data*, https://data.worldbank.org/indicator/GC.TAX.TOTL.GD.ZS?most_recent_value_desc=false&view=map (last

GDP and hence a little helping hand from the corporates should be welcome but this argument often overlooks the fact that the ratio is actually on par with other emerging economies and that India has one of the highest corporate tax rates in the World.[51]

The CSR provision in the Act has definitely increased the number of companies participating in corporate philanthropy thus introducing those companies to the benefits associated with undertaking CSR initiatives who would have never even considered engaging in philanthropic work. Now even if the CSR provision is to be struck down, there is a greater possibility that these companies will still voluntarily continue to engage in CSR.

The CSR provision is also in conformity with the country's constitutional values. It is important in achieving the constitutional objectives as stated in the preamble viz. justice, liberty, equality and fraternity.[52] Article 21 guarantees right of life and liberty.[53] Right of life is considered very wide and far reaching in its ambit so much so that even right of livelihood has been included in it by the Supreme court in Olga Tellis v. Bombay Municipal Corporation[54]. It is thus the moral responsibility of companies to secure the right to life and livelihood of the financially weaker section of the society. The Directive Principles of State Policy reiterate the object of the country by including principles such as *"the citizens, men and women equally, have the right to an adequate means of livelihood"[55], "the ownership and control of the material resources of the community are so distributed as best to subserve the common good"[56], "the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment"[57]* etc. and CSR is required to achieve those. The courts too have time and again ruled that companies have a responsibility towards the society as well Eg.it has been held by the Supreme Court as far back as 1950 that companies have a social character and must not worry only for the individuals who put their money in it[58], the Bombay High Court has held that businesses don't merely exist for the welfare of shareholders but for their employees and their customers as well[59]

visited April 7, 2020)

[51]KPMG, *Tax Rates Tool Test Page*, https://home.kpmg/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online/corporate-tax-rates-table.html (last visited April 17, 2020)

[52] INDIA CONST. pmbl.

[53] INDIA CONST. art. 21

[54]Olga Tellis v. Bombay Municipal Corporation (1985) 2 SCR Supl. 51 (India)

[55] INDIA CONST. art. 39, cl. (a)

[56] INDIA CONST. art. 39, cl. (b)

[57] INDIA CONST. art. 39, cl. (c)

[58]Chiranjit Lal Chowdhuri v. The Union of India (1950) SCR 869

[59]The Saraswat Co-Operative Bank v. P.G. Koranne (1983) 85 BOMLR 134 (India)

IV. Problems associated with mandatory CSR

There are definitely numerous advantages of CSR but do the benefits outweigh the costs?

Section I of this article introduced us to the current provisions of CSR in India and also highlighted many fallacies pertaining to it. Thereby lies the biggest problem of mandatory CSR. It is almost impossible to frame laws directing charity. Most companies will always see CSR as a cost to their company and will try to avoid it by finding loopholes in the law regardless of how bulletproof the law is framed. Charity is something that cannot be mandated and therefore mandatory CSR is problematic at the legislative stage itself. It is equally difficult to regulate it. The companies who genuinely undertake CSR initiatives will always be at a disadvantage compared to the ones who try to find a way around it. It has already been seen how easy it is for politics to highjack CSR. The only possible solution to this is to have a rigid system of directives applicable to all but that will kill the creativity and the 'out of the box thinking' involved in it which otherwise has always been exercised by companies in their charitable endowments since before the addition of the provision.

Companies are first accountable to their direct stakeholders such as shareholders (including small shareholders and the general public in case of public companies who put in their hard-earned money and savings into buying shares), depositors, creditors, employees, suppliers and the locality they are situated in before anybody else. Companies being mandated to spend 2% of their average net profits is essentially taking away the amount from these direct stakeholders, meaning that CSR is being done at the cost of their wellbeing. It makes no sense to make companies spend money to be called socially responsible when they don't pay their employees well or when they have a high amount of debt and sadly none of these factors are taken into consideration. This is a serious dichotomy. The money spent on CSR can instead be used in strengthening the financial condition of the company by focusing on internal issues to better meet its business objectives resulting in a stronger economy, benefitting all. There is close to no evidence showing charity solving problems of a country but economic growth sure has. The companies should instead have the liberty to take up CSR initiatives when they are doing well and skip them when they are not. The Proposed Bill does allow this flexibility to some extent by allowing companies that spend an amount in excess of the requirement to set off such excess amount against the requirement of successive financial years.[60]

The role of the government is to provide basic services like healthcare, primary education etc. across the board in a non-discriminatory manner while the role of companies is essentially to

[60] The Companies (Amendment) Bill, No. 88 of 2020, § 27 (as introduced in Lok Sabha)

generate profit and wealth for an economy in a more sustainable, law abiding and ethical way and the role of charity is to close the gap via individual voluntary charity. By compelling the companies to do the government's job hardly seems fair. Government's spending is scrutinised at every step with a great deal of transparency. The same kind of check cannot be put on companies hence allowing leakages in the system as has been pointed out in section I earlier. The government can be held accountable for every penny they spend and be punished for misallocation of funds if their projects fail, if not by law then through elections. Since companies cannot be held up to the same standard as the government, it's fruitless to make them do the government's work.

However, the biggest problem with mandatory CSR as per the Act is that funds that could be allocated to improve internal issues are being diverted to external activities. This point has been discussed on several occasions throughout the paper. A company causing immense pollution cannot be allowed to hide behind its CSR initiative of planting trees. Something in line of China's Environment Protection Tax[61], taxing companies for discharge of pollutants and generation of solid waste can be a more effective tool as it provides an incentive to companies to innovate and reduce their carbon footprint. In such cases CSR does very little to benefit the society. The society would be better off in the long run if the company is able to invest the CSR money in its internal research and development to come up with solutions for reducing its levels of pollution. Eg. BP plc's sponsorship of the National Portrait Gallery[62] and the British museum[63] was met with strong protests due to the company's questionable environmental track record. Within months, the company pledged to cut its greenhouse gas emissions to net-zero by 2050.[64]This sponsorship would be recognized as a CSR activity in India.

V. SUGGESTIONS

If there has to be mandatory CSR then it needs to be restricted to companies operating in industries that are known to create significant negative externalities such as pollution, depletion of resources, social upheaval etc. The idea is to offset the damage caused and to increase their

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[61]Chen Jia, *Environmental tax to help China fight pollution*, China Daily (November 1, 2018, 06:54) http://www.chinadaily.com.cn/a/201801/11/WS5a5699b7a3102e5b173740b4.html#:~:text=China%20will%20levy%20tax%20on,into%20effect%20on%20Jan%201.&text=%22To%20increase%20fiscal%20income%20is,the%20tax%2C%22%20he%20added

[62]Mattha Busby, *Semi-Naked Activists Protest Against National Portrait Gallery's Links With* BP, The Guardian (October 20, 2019, 17:26 BST) https://www.theguardian.com/artanddesign/2019/oct/20/semi-naked-activists-protest-national-portrait-gallery-bp-sponsorship-fake-oil-extinction-rebellion

[63]Mathew Taylor, *British Museum Staff Join Outcry Against BP Sponsorship*, The Guardian (February 10, 2020, 14:00 GMT) https://www.theguardian.com/culture/2020/feb/10/british-museum-staff-join-outcry-against-bp-sponsorship

[64]Anjili Raval, *New BP Boss Bernard Looney Pledges Net Zero Carbon Emissions By 2050*, Financial Times (February 13, 2020) https://www.ft.com/content/e1ee8ab4-4d89-11ea-95a0-43d18ec715f5

acceptance by the inhabitants of the areas they are based in. Industries generally falling under this head are the ones associated with mining, production plants that require a lot of water, tobacco etc. Looking at the mining industry in particular, it is one industry that is always under criticism for its impact on the environment and the displacement of local inhabitants. As a result, The Mines And Minerals (Development And Regulation) Act, 1957[65] read with Mines and Minerals (Contribution to District Mineral Foundation) Rules, 2015 includes a provision requiring mining lease holders to contribute 10% (in respect of mining leases granted on or after 12th January, 2015) or 30% (in respect of mining leases granted before 12th January, 2015)[66]of the royalty they are paying with respect to the mining lease, to a trust known as the District Mineral Foundation established by the State Governments. The funds so collected are to be used for the interest and benefit of persons, and areas affected by mining related operations. Eg. The trust established by the Jharkhand Government had spent INR 751.23 Crores by 31st December 2018 for FY 2018-2019 on drinking water and sanitation based development in districts affected by mining related activities.[67]Thus the external CSR as intended by the Companies Act, 2013 should be limited to companies involved in industries identified to create negative externalities. Article 74 of Law No. 40 of 2007 on Limited Liability Companies as applicable in Indonesia puts the onus of performing budgeted Social and Environmental Responsibility on companies having their business activities in the field of and/or related to natural resources.[68] However the implementation of Article 74 suffers from the lack of a definition for Social and Environmental Responsibility[69] but that is a problem that can be overcome to a certain extent and be adopted in the Indian context as mentioned above.

A subtle way of implementing CSR and compelling companies to undertake CSR initiatives is by putting the onus of pressuring the companies on institutional investors rather than the legislation mandating CSR. Institutional investors such as mutual funds can be asked to take into consideration the CSR initiatives undertaken by a company as one of the factors deciding investment in those companies. Indonesia has a provision stipulating that investors (both domestic and international) have an obligation to *"meet corporate social obligations; respect the traditions and culture of the society around where the capital investment activities are*

[65]Mines and Minerals (Development and Regulation) Act, No. 67 of 1957, Acts of Parliament § 9B (inserted by Act 10 of 2015) (India)

[66]Mines And Minerals (Contribution To District Mineral Foundation) Rules, 2015, Gazette pt. II sec. 3(i) (Oct. 20, 2015)

[67]Government of Jharkhand, *District Mineral Foundation Data,* https://mines.gov.in/writereaddata/UploadFile/DMFJharkhand18012019.pdf (last visited April 01, 2020).

[68] LAW No. 40 OF 2007 Concerning Limited Liability Company of the Republic of Indonesia. Ar.74 (Indon.).

[69]Armand Maris, *Compulsory CSR: Indonesia Takes A Tough Stance But Clarity On Definitions Is Lacking*, IPRA Thought Leadership essays (2015) https://www.ipra.org/news/itle/compulsory-csr-indonesia-takes-a-tough-stance-but-clarity-on-definitions-is-lacking/

conducted;"[70] and have a responsibility to *"create a healthy business competition climate, guard against monopolistic practices and other activities that cause loss to the state; preserve the living environment; create safety, health, comfort and welfare for workers;"*[71]This provision however suffers from a lack of clarity and definitions but the same can be framed properly and adopted in India to suit our aims and objectives. Likewise several European countries require their pension funds to disclose the social, environmental and ethical factors taken into consideration while making an investment.[72] By limiting investments the institutional investors can make to companies that conduct CSR in accordance with Section 135 of the Act, the companies will be incentivised rather than forced to undertake CSR initiatives. It is recommended that this provision be limited to domestic institutional investors only and not foreign institutional investors to avoid discouraging investments in India.

For effective implementation of CSR, it is important that it be externally reviewed. Credit rating agencies can perhaps take up the job of rating companies' CSR initiatives as per guidelines to be issued in this regard. This will increase accountability on behalf of companies and also allow investors to make an informed decision. Institutional investors too will find it easier to distinguish socially responsible companies and will not have to do the diligence themselves. There can even be a threshold rating for companies to be qualified to get investments from these institutional investors.

For reasons discussed in the previous section, focus should be on internal issues and the money earmarked for CSR should be spent on reducing negative externalities being generated in due course of business, welfare of employees earning the least amount of income, sustainable practices, ethical behaviour in its operations etc. while external charity should be left to be voluntary with incentives to encourage it. This is in fact how CSR is perceived over the globe. While the Act puts a fiduciary duty on directors to act in the best interests of *"of the company, its employees, the shareholders, the community and for the protection of environment."*[73], its not strong enough to serve much of its purpose. Additionally, the Ministry of Corporate affairs' National Guidelines On Responsible Business Conduct[74]assist businesses in conducting their business in an ethical way creating positive externalities for all the stakeholders by inculcating ESG norms, however these are merely guidelines and not binding. Securities and Exchange

[70] Law No. 25 OF 2007 Concerning Capital Investment Of The Republic of Indonesia. Ar.15 (Indon.)
[71]Law No. 25 OF 2007 Concerning Capital Investment Of The Republic of Indonesia. Ar.16 (Indon.)
[72]Güler Aras & David Crowther, A Handbook Of Corporate Governance And Social Responsibility, 399-401, 2010
[73] Companies Act, 2013, No. 18 of 2013, Acts of Parliament § 166(2) (India)
[74]Ministry of Corporate Affairs, *National Guidelines On Responsible Business Conduct*, https://www.mca.gov.in/Ministry/pdf/NationalGuildeline_15032019.pdf (India)

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Board of India has taken a stronger approach by mandating the top 1000 listed companies (based on market capitalization) to disclose the initiatives taken by them from an environmental, social and governance perspective as Business Responsibility Reports in their Annual reports.[75]A more detailed CSR report dealing with internal initiatives, similar to a Business Responsibility Report, can be extended to companies falling under the application of Section 135 of the Act. For further scrutiny, the report can be eligible for audit by the auditors instead of just being disclosed in the Board's Report.

Other possible solutions could include a 3 years moratorium exempting them from CSR expenditure for newly incorporated companies, conducting impact assessment studies for CSR initiatives undertaken, increasing threshold that qualifies companies to fall under section 135 as the current amount ends up including comparatively smaller companies who are even less likely to gain from the publicity that CSR brings, making CSR mandatory only for a few years to inculcate the habit of philanthropy in companies and then providing incentives to encourage them to voluntarily continue their practices and encouraging philanthropy at the hands of shareholders instead. The high committee report suggests extension of CSR provisions to LLPs, Partnerships, Banks registered under the Banking Regulation Act, 1949, companies formed under parliamentary acts etc. as well to ensure a level playing field.[76] This in fact has been done in China as the provision[77] mentioned in section I of this paper has been inculcated in the country's 2007 Partnership Enterprise Law.[78] The committee has also recommended conducting an annual CSR survey in line with Economic Survey and other Sectoral Surveys to identify the trends and gaps.[79]

VI. CONCLUDING REMARKS

CSR is a desirable tool for any economy to progress in a holistic way and more so in a country riddled with vast social economic disparities. Despite this, most of the countries have either shied away from implementing it or have limited its scope to disclosures. Although CSR law appears indispensable, it is too ambitious owing to the difficulty in defining it in statutory terms rendering it too vague to be operational. It is equally difficult to provide remedies for noncompliance. The current provision of law has so far not been tested enough in the courts

[75]Listing Obligations And Disclosure Requirements) Regulations, 2015, Gazette pt. III sec. 4, Rule 34(2)(f) (September 2, 2015)
[76]See supra note 17
[77] See supra note 34
[78][Partnership Enterprises Law Of The People's Republic Of China] (Promulgated by Standing Comm. of the Nat'l. People's Cong, February 23, 1997, revision effective August 27, 2006, art. 7
[79]See supra note 17

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yet but its interpretation is sure to place high demands on the judiciary.

By diverting the resources from internal overhauls to external projects is not going to do much for the company or the society whose welfare is the objective behind the provision. CSR can only be successful when it is rewarded by financial markets. This is more likely to be achieved when companies are encouraged to focus on their internal shortcomings through innovation.

The current CSR regime in India is riddled with fallacies and needs serious reconsideration at all levels. The need of the hour is to re-evaluate the present regime and figure out creative ways to solve the social issues with voluntary support from the companies.

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