Acting Responsibly

The Companies Act of 2013

On 29 August 2013,India became the first country to mandate reporting on corporate social spending by passing the Companies Act with the assent of both Parliament and the President.

Over the last few decades, corporate social responsibility (CSR) has seen a surge in popularity in westernized countries and India alike. CSR is by no means a new phenomenon, and several national governments and international bodies have worked to encourage CSR investment by the private sector. Countries as diverse as the Philippines, Thailand, Italy, and Canada have policies to encourage responsible business practices. On an international scale, the United Nations Global Compact was established in 2000 to coordinate a global push towards voluntary CSR practices among its signatories.

The Companies Act of 2013 only mandates CSR reporting on the part of the private sector, yet the hope is that the public dissemination of CSR spending information will effectively obligate corporate contributions. Previous legislation from the Government of India – namely the Department of Public Enterprises' "Guidelines on Corporate Social Responsibility and Sustain ability for Central Public Sector Enterprises, 2010" – has also required percentage contributions to CSR activities from large central public sector enterprises for several years. Even as we analyze the implications and lingering questions about the Companies Act, it is important to recognize that India has broken new ground and therefore lacks international precedents that it can learn from.

A Growing Corporate Role

The Government of India is the country's primary provider of social services and development initiatives, implementing programs in education, healthcare, poverty alleviation and social welfare. Although gross expenditure in these and other related areas is enormous, the government's social spending as a proportion of GDP still falls far short of those of other highly developed countries. Furthermore, despite its best efforts to improve, the pace of government-led social development is often viewed as stagnant and unable to reach key target populations. The Indian government is therefore constantly faulted with under investing in health and education, particularly in light of the nation's economic growth, high GINI coefficient of inequality and low Human Development Index, as well as the potential resources it *could* be funneling toward these sectors. At the same time, international donor involvement in India has been diminishing, with bilateral donors such as the British Department for International Development (DFID) reducing the amount of aid to India in response to the country's movement towards a middle class ranking.

Companies Act of 2013

Section 135 of the Act states that companies having net worth of INR 5000 million or more, or turnover of INR 10,000 million or more, or a net profit of INR 50 million or more during any financial year shall spend 2% of the company's average net profits before tax from the previous three years on CSR. Schedule VII of the Act specifies nine general areas to which funds could be donated, and while pursuing CSR activities is not legally mandatory, reporting on spending is.

Despite the inadequacies of state social development, India's economy is in the midst of a relative boom. The private sector has come to dominate the Indian psyche, with its share in the net manufacturing and services sales growing from 48.8% in the 2000-01 year to 68.5% in 2009-10. This amounts to corporate profits of roughly INR 6 trillion per year.

In the wake of the Companies Act 2013, a March 2013 study by Forbes and CSRidentity.com has projected a potential annual availability of INR 56,110 million towards eligible non-government organizations (NGOs) and other charitable purposes by India's top 100 companies. This is a significant jump from the INR 17,650 million that the same firms are currently spending. Similar estimates put the total potential CSR funding for all eligible Indian companies at INR 120,000 million for the top 1000 companies for the first year, with funding projected to be INR 170,000 million after the initial few years. Nevertheless, while impressive, it is important to note that this sum is still a tiny fraction of the government budget; the Department of Rural Development alone spends INR 700,000 million per annum. Measures such as the Companies Act are thus best viewed as a catalyst for further corporate sector involvement in social development.

Whose Money Is It?

Although the Companies Act of 2013 was enacted with the interest of social development in mind, the legislation raises questions about the Indian government's encroachment into capitalist territory. At the heart of corporate disgruntlement regarding the Act is the belief that in a free economy, businesses should be able to spend their profits as they see fit.

The Government of India has already set precedents of imposing 'cess' or earmarked temporary taxes designed to raise money for a particular cause, such as the 3% education cess. Would it not be equally effective to simply increase taxes on the same top companies by 2% and allow the government to manage earmarked incoming funds by funneling them to social development departments?

Two factors are relatively unique to India and may have been influential in deciding why Section 135 of the Companies Act took the format of directed spending rather than increased taxes. The first factor is that despite relatively low government social spending, India is still considered to be a socialist state, not a purely capitalist society. Unlike countries like the United States in which the government takes a largely hands-off approach towards private regulation, in the Indian context, there remains room for debate about the acceptability of the Companies Act's mandate. In an article in the Asian-Pacific Law & Policy Journal, Van Zile argues that the Indian government's decision regarding CSR is actually "a rational response to a major tension in the Indian economy" and a logical way for the state to support economic equality while avoiding suffocating regulation. It will be particularly interesting to see if the Companies Act of 2013 shifts the dynamic between the Indian government and businesses.

The second factor is the avowed emphasis on keeping the new flow of private CSR funds away from the government and its existing initiatives. Dr. B Chatterjee, Director General and CEO of the Indian Institute of Corporate Affairs that helped the Ministry of Corporate Affairs to frame the Companies Act, has explicitly encouraged the private sector to avoid simply channeling funds towards government activities such as the Prime Minister's National Relief Fund, even if that route would be easier. Such exhortations take the opinion that individual corporate decisions about how and where to invest in social development projects may prove to be more effective and innovative than current government practices in addressing marginalized populations.

What Counts as CSR?

Despite the guidelines recently laid out in the Companies Act, the fundamental question of 'what is corporate social responsibility?' still lacks a definitive answer. Businessmen, policymakers, and think tanks have disputed the exact definition of CSR for years, and despite the slew of literature on the subject, each sector seems to hold a different perspective.

CSR in Europe and the United States has tended to focus on voluntary compliance with ethical and responsible business practices. These include but are not limited to pursuing more environmentally-friendly work practices, minimizing the negative impact of factories and businesses on surrounding communities, and ethical labor relations, all of which serve to remind corporates that they belong to a larger society that feels the implications of their work.

Yet for the corporate sector in India, CSR has historically been affiliated with philanthropy on the part of highly successful Indian companies, with the most prominent examples including the Tata Group and the Aditya Birla Group. In recent years, firms have found other reasons to incorporate CSR strategies into their company policies, in particular to (i) improve their public brand image and develop a loyal customer base in light of business competition, (ii) rationalize their growing size and wealth in a nation where millions lack basic necessities, and (iii) respond to the vast majority of consumers who believe that CSR should be mandatory for Indian companies. These policies almost exclusively center on the establishment of private trusts or foundations or donations to external community development organizations, completely bypassing spends on internal company labor – the very emphasis of CSR in the West.

In the Companies Act, the Indian government attempts to lay forth a new definition of CSR. However, despite these efforts to create a definitive set of guidelines, much further clarification is needed on what counts as CSR in the Act and whether the Act's guidelines are justifiable. For example, catch all clauses such as "such other matters as may be prescribed" leave ambiguity as to whether the socially-driven activity of religious organizations or political participation campaigns may be supported by corporates under the Act. The Act noticeably avoids supporting good internal business practices, such as business ethics, worker rights, or environmental sustainability, raising concerns that these issues will be overlooked in an attempt to donate to external development projects that may have far less long-term impact. Avoiding these issues may result in superficial company commitments to CSR, which implies that the Companies Act may actually be counterproductive in advancing the dialogue around socially responsible corporate activities.

(Mis)Communication Across Sectors

The inability of the different sectors to agree upon a common definition of CSR is part of a greater problem of communication and mistrust that clouds conversations across the sectors. The deficit of trust between the corporate and development sectors has long been recognized as a barrier to expanded private-NGO partnerships, and although efforts have been made to improve transparency and accountability by encouraging regular NGO reporting, it is essential to understand whythis deficit still exists and where misunderstandings lie.

One barrier to mutual trust is the fact that every sector has a different motive for its work, which often inhibits complete understanding of the others. Although the grossest stereotypes – NGOs want to 'serve', the private sector to 'make a profit', and the government to 'regulate' – may seem extreme, these do explain the drivers of action for many members of these sectors. When all three sectors are required to collaborate, as is now the case with CSR in India, frustrations are quick to arise. For example, one common corporate perception is that the government does not understand the idea that profits are necessary to insure against risk, particularly in light of external socioeconomic variables that affect business but cannot be internally controlled. And government functionaries can be judged to be unnecessarily nitpicking and hidebound. Open dialogues are required to discuss hoped for results from CSR before it can be pursued in a trustful atmosphere.

A second barrier is the different language used to describe work by the different sectors, with discrepancies in rhetoric even affecting the effectiveness of CSR activities. As with the motives, concrete conclusions must be made about the language surrounding CSR and how its connotations affect the success of private-public-NGO partnerships. The working relationship is perceived in contrasting ways by the different sectors; for example, NGOs want a 'partnership' that connotes equality in position, whereas corporates interested in CSR prefer to frame themselves as a benevolent 'donor'. This difference in rhetoric and connoted priorities can also make assessment of the impact of CSR activities difficult. For example, C Squires of Marie Stopes International has noted that indicators of CSR impact – whether in the field of health, education, or environmentalism – vary greatly, and the sum of small disagreements like these can impede budding relationships between the sectors.

The greatest barrier to CSR activity remains a perceived lack of transparency and financial accountability on the part of the NGO recipients. Even in 2013, 60% of private donors received no regular communications about the impact of their donations, though 26% would give more money if reporting by the nonprofit were improved. Some measures have been established to improve corporate-nonprofit relations in this regard. The emphasis placed on regular monitoring reports by the Companies Act, the Securities and Exchange Board of India, and other organizations will hopefully address this gap, while a set of NGO accrediting agencies such as the Credibility Alliance and Give India are part of a larger campaign to improve transparency and accountability from the nonprofit sector. This will be particularly important for the future of CSR relationships since it allows distinctions and educated investments to be made among the more than 3 million registered NGOs in India.

Conclusion

Despite the excitement surrounding the promulgation of the Companies Act 2013, it is clear that several conversations remain to be had on the role of CSR in India's social development. The questions raised in this paper are only a few of those that must be answered before effective corporate-NGO partnerships and supportive government guidance can be developed. It goes without saying that finding a concrete solution to even one of these challenges will be complicated, and moving forward will require careful thought and reevaluation of the field of CSR.

Over the next few decades, the definition and prominence of corporate social responsibility across the world will continue to evolve as India and other nations experiment with CSR policies at both government and corporate levels. Considering the diverse stakeholders involved in designing and implementing CSR activities, it will be essential to consider the involvement of each sector of society and remain open to novel ideas in order to establish an effective CSR framework. Teamwork and collaboration will be the cornerstone of reform, rather than rhetoric that focuses on philanthropy alone.

Implementation of the Companies Act of 2013 will begin in April 2014 and will bring a new wave of discussion and new set of lessons, and will hopefully pave the way to more effective corporate social responsibility in India. However, in the end, the Companies Act is just one step in the process towards a strong CSR dialogue in India – albeit a necessary step – and policymakers and businessmen alike must build on its momentum to move forward.

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This background has been used by Amaltas on its work in Springbox- an initiative by Amaltas to build responsible relationships between corporates and NGOs to act in unison to create standards of practice, support pathlighter ideas and work with the marginalized in our society.