Indian Companies Act, 2013 – Changing the face of CSR in India

The Indian Companies Act, 2013, is the first of its kind in the world. One of the most applauded aspects of the new Company Law regime is the mandatory corporate social responsibility (CSR) spending requirement, which is governed by Section 135 of the act. The CSR provision would change the way Indian corporates do business because till now CSR has largely been a voluntary contribution by corporates. The choices we make today are going to influence our generations to come. This provision can make CSR a driver of capital formation in neglected areas of national interest as India is a fast-growing emerging economy but also faces numerous human development challenges. It is clear that there will be an immense flow of funds and this flow will help companies effect the pressing societal challenges, but a disciplined approach is necessary so that companies can make an unprecedented contribution to India’s future. This paper makes an attempt to understand the provisions of Section 135 of the new Companies Act, 2013, its implications and implementation. It also studies the spending patterns before the implementation of the act and the henceforth expected change.

Introduction

The Indian Companies Act, 2013, the first of its kind in the world, redefines the landscape of the Indian social sector, heralding a new era on the path to inclusive growth (FICCI–Accenture 2014). One of the most applauded aspects of the new Company Law regime is the mandatory social spending requirement (corporate social responsibility, CSR) governed by Section 135 of the act. Faced with innumerable economic and social challenges as our country is, our lawmakers could not have ushered in a more revolutionary change through the new law (Vaidyanathan & Thacker 2014). The CSR provision would change the way Indian corporates do business because till now CSR has largely been a voluntary contribution by corporates (Grant Thornton). Even as many companies have been reaching out to the underprivileged for decades, driven by the trusteeship concept, there are several organisations that have not been engaged in the community development space (FICCI–Accenture 2014). For the first time in India, CSR has become a concrete resource allocation platform backed by legislative support. The new law presents several opportunities for Indian companies to not only strengthen their CSR efforts but also shape India’s economic future and their own global competitiveness (FICCI–Accenture 2014). The choices we make today are going to influence our generations to come. The inclusion of the CSR mandate is an attempt to supplement the government’s efforts of equitably delivering the benefits of growth and to engage the corporate world with the country’s development agenda (PWC 2013). This provision can make CSR a driver of capital formation in neglected areas of national interest as India is a fast-growing emerging economy but also faces numerous human development challenges. These include maternal health problems, infant mortality and intractable diseases such as malaria and tuberculosis (FICCI–Accenture 2014). Take maternal health for instance, India and Nigeria accounted for one third of global maternal deaths in 2013. An estimated 50 000 maternal deaths occurred in India in 2013. Although India has been able to substantively reduce its maternal mortality rate (MMR), India runs the risk of missing the MMR target set under the auspices of the Millennium Development Goals. While the government is launching extensive interventions, it is evident that more efforts need to be taken to achieve the desired MMR targets. The CSR Rules 2014 provide an opportunity to corporations to work with public agencies and help the nation achieve the desired MMR targets (FICCI–Accenture 2014).

CSR is the continuing commitment by business to contribute to economic development while improving the quality of life of the workforce and their families as well as of the community and society at large (WBCSD). The UNIDO defines CSR as a management concept whereby companies integrate social and environmental concerns in their business operations and interactions with their stakeholders. CSR is generally understood as being the way through which a company achieves a balance of economic, environmental and social imperatives (‘triple-bottom-line approach’), while...
addressing the expectations of shareholders and stakeholders. In this sense, it is important to draw a distinction between CSR, which can be a strategic business management concept, and charity, sponsorships or philanthropy. Even though the latter can also make a valuable contribution to poverty reduction, directly enhance the reputation of a company and strengthen its brand, the concept of CSR clearly goes beyond that (UNIDO). Today, CSR has become a worldwide concept whereby organisations consider the interests of society by taking responsibility for the impact of their activities on customers, employees, shareholders, communities and the environment in all aspects of their operations. It is one of the most important global issues with serious challenges and implications on almost all sectors. Surging economies, including India, are coping with issues related to poverty, child rights, community welfare etc. and are a hotbed for an innovative CSR Scenario, which is still shaping up (KPMG & ASSOCHAM 2008).

CSR – Global scenario

‘India would become the first country to mandate corporate social responsibility (CSR) through a statutory provision’, said Mr. Sachin Pilot, ex- Corporate Affairs Minister (KPMG 2014).

Social and economic initiatives, as a responsibility of the companies, are gaining popularity internationally. The Financial Reporting Council in the United Kingdom is in the process of introducing guidelines for disclosures regarding environmental, social and governance issues by a company. The intention is for these to replace the existing ‘business review’ section of annual reports, and companies would be required to provide complete disclosure about their business activities, including social efforts (Vaidyanathan & Thacker 2014). In India, the concept of CSR is governed by Section 135 of the Companies Act, which was passed on 29 August 2013. The CSR provisions within the act are applicable to companies with an annual turnover of Rs. 1000 crores and more, or a net worth of Rs. 500 crores and more, or a net profit of Rs. 5 crores and more. The act encourages companies to spend at least 2% of their average net profit of the previous 3 years on CSR activities, such as eradicating extreme hunger and poverty; promoting education; promoting gender equality and empowering women; reducing child mortality and improving maternal health; combating human immunodeficiency virus (HIV), acquired immune deficiency syndrome (AIDS), malaria and other diseases; ensuring environmental sustainability; providing employment-enhancing vocational skills; funding social business projects; contributing to the Prime Minister’s National Relief Fund or any other fund set up by the central government or the state governments for socio-economic development and relief and funds for the welfare of the scheduled castes, the scheduled tribes, other backward classes, minorities and women; and such other matters as may be prescribed (Grant Thornton).

Companies can also collaborate with each other for jointly undertaking CSR activities, provided that each of the companies are able to individually report on such projects (Bahl 2014). The new rules will be applicable from the fiscal year 2014–2015 onwards (PWC 2013). The act lists out a set of activities eligible under CSR (PWC 2013). The 2013 act stipulates that the company shall give preference to the local area and areas where it operates (Grant Thornton). The CSR activities should not be undertaken in the normal course of business and must be with respect to any of the activities mentioned in Schedule VII of the 2013 act. Contribution to any political party is not considered to be a CSR activity, and only activities in India would be considered for computing CSR expenditure (Bahl 2014). Also, activities meant exclusively for employees and their families will not qualify (PWC 2013).

CSR spending in India on various activities (before the new act)

The FICCI–Accenture Report conducted in-depth conversations with 30 senior leaders from companies and civil society organisations to understand the industry response to this changing CSR environment; this was complemented with a survey of 20 companies (FICCI–Accenture 2014). These discussions revealed the growing understanding within businesses towards leveraging CSR as a platform to initiate actions benefiting their business as well as the nation. Most large- and medium-sized companies are viewing CSR initiatives as their contribution to the developmental agenda.

| Table 1: CSR spending requirements. |
|------------------------------------|
| **Sr. No.** | **Country** | **Whether CSR spending/reporting mandatory** |
| --- | --- | --- |
| **Countries not having mandatory guidelines for CSR spending/reporting** | | |
| 1. | UK | Voluntary guidelines in place for CSR reporting |
| 2. | USA | Voluntary reporting by companies in sustainability reports |
| 3. | China | Voluntary reporting by companies in sustainability reports |
| 4. | Germany | Voluntary reporting by companies in sustainability reports |
| 5. | Australia | Voluntary reporting by companies in sustainability reports |
| **Countries having mandatory guidelines for CSR spending/reporting** | | |
| 1. | France | Mandatory reporting for listed companies in annual reports on CSR activities |
| 2. | Denmark | Investors and state-owned companies to include information on CSR in their annual financial reports |
| 3. | Sweden | Mandatory reporting by state-owned companies |
| 4. | Indonesia | Natural resource-based companies must allocate budgets for CSR programmes and the programmes must be run according to government regulations |
| 5. | Malaysia | Compulsory for companies listed on Bursa Malaysia to disclose their CSR activities or practices |

Source: KPMG, 2014, ‘CSR in India – A changing landscape’, Report, March 2014.
of the society, rather than simply as efforts that grant them a ‘license to operate’ (FICCI–Accenture 2014).

A study of the CSR activities undertaken by the top 200 firms in the year 2012–2013 across 10 industries attempts to get an industry-level analysis of the nature of these activities (Bansal & Rai 2014).

Most of the firms undertake CSR expenditure for the welfare of the rural communities (Table 2), especially around their areas of operation. A possible reason could be to generate goodwill amongst people in the neighbourhood and become familiar with the area and its needs, which, in turn, would minimise costs of providing services. Contrary to the developed countries where CSR activities are undertaken mainly in the area of environment, in India it is mainly undertaken in the social sector (Bansal & Rai 2014). In the light of the recent legislation, it would be interesting to see how companies would change their CSR strategies. After community development, education (including skill development) attracts the largest share of CSR expenditure. Health is also a major area where firms like to invest (Bansal & Rai 2014).

### Implications of Companies Act, 2013 (CSR)

An increasing number of businesses, high-net-worth individuals and mid-tier professionals want to contribute to societal growth through active engagement. These organisations and individuals have significant resources and experience and are no longer interested in ‘cheque philanthropy’. They are ready to play a far more active role in shaping growth trajectories of institutions and accelerating social change (FICCI–Accenture 2014).

According to the Indian Institute of Corporate Affairs (IICA), about Rs. 200 billion (roughly US$ 3.2 billion) could be unlocked from a pool of around 16 000 companies for CSR spending during 2014–2015 (FICCI–Accenture 2014). CSR initiatives in Indian companies stand to benefit tremendously, thanks to significantly more predictable spending (FICCI–Accenture 2014) (see Table 3).

### Companies allocating percentage of their PAT each year for CSR activities: Businesses capitalise on natural, social, human and economic resources to have the long-term perspective such that future is sustainable and stable. They need to make sustainability a core driver of their strategy. The real challenge, however, lies in the widespread adoption of these initiatives. The ‘Business Responsibility: India Survey, 2013’ helps to understand where the initiatives stood before the implementation of the new act (India Survey 2013). The surveyed companies include the top 200 companies by market capitalisation, and the survey was conducted using a questionnaire technique (India Survey 2013).

Sixty-five per cent of the respondents claim to allocate a certain percentage of their PAT each year for CSR activities (Figure 1). Of these, about 25% companies commit at least 2% of their PAT on CSR activities. About the same percentage of companies claims to spend up to 2%. Almost 12% companies suggest that their CSR budget varies between years and are dependent on projects (India Survey 2013).

### Expected increase in CSR expenditure and reporting: Forbes India survey realised that many firms, even among the top 100 firms by revenue (FY 2012), do not report their CSR expenditure or even declare the social causes they support, as they are not required to do so by law. But all this will change now that the new Companies Act, 2013, requires formal reporting of CSR efforts by corporates. The data pack, compiled by CSRidentity.com, together with Forbes India, tells you how much each company will have to fork out on CSR, once they are bound by law (Jayashankar, Paul & Bhat 2013).
Implementation of the act

The CSR regime complements the efforts of the government and non-government organisations by requiring companies in India to initiate activities for the economic wellbeing of the underprivileged and for the environment. Companies can also join hands to undertake CSR projects (Vaidyanathan & Thacker 2014). Experts say that these companies should outsource the CSR activities to civil society sector instead of creating an army of people for carrying out the CSR activities. They should allow not for profit companies to actually execute the programme at the ground level (Business Standard 2015).

When a company chooses an initiative that fits its values and purpose, it should commit managerial talent to the chosen problem, and should address it just as it would do in a business situation (Kasturi Rangan 2014). A company should carefully choose the activities where it can bring its resources and competence to play. An engineering company is likely to have better skills at addressing problems of lack of sanitation, a software company might have better skills at addressing education and a consumer goods company would be better at addressing public health and hygiene issues (Kasturi Rangan 2014). Every company should attempt to move the needle on the social or environmental problem it undertakes. Big companies, by bringing their technical and organisational skills to bear, not just money, should attempt to uplift the capability of their social value chain partners (this often will be the local government) and make a real dent on the problem.

Analysis of CSR activities of top 100 companies shows that the mode of giving has primarily been through non-government organisations and other social organisations as around 90% (Figure 2) companies are channelling their funds through them (FICCI–Accenture 2014). While majority of companies have established in-house foundations to engage in social activities, around 10% of the organisations choose to design and execute activities directly through them.

Conclusion

A robust and thriving development sector is central to India’s quest for equitable, inclusive and sustainable growth (PWC 2013). The Indian Companies Act, 2013, marks a paradigm shift in India’s corporate law regime and has far-reaching implications for both domestic companies and overseas investors with a presence in India (Shroff 2014). India’s development sector

| Sr. No. | Company                     | Revenue (FY 2012) | Avgas PAT | Actual spend | 2% of PAT |
|---------|-----------------------------|-------------------|-----------|--------------|-----------|
| 1.      | Indian Oil Corporation (IOC)| 442 459           | 7783      | 83           | 156       |
| 2.      | Reliance Industries         | 368 571           | 21 138    | 288          | 423       |
| 3.      | Bharat Petroleum Corporation| 223 315           | 1438      | 8            | 29        |
| 4.      | Hindustan Petroleum Corporation| 195 891         | 1118      | 27           | 22        |
| 5.      | Tata Motors                 | 170 678           | 8437      | 15           | 169       |
| 6.      | Oil & Natural Gas Corporation (ONGC)| 151 121   | 23 660    | 121          | 473       |
| 7.      | State Bank of India (SBI)   | 147 197           | 13 056    | 71           | 261       |
| 8.      | Tata Steel                  | 135 976           | 3895      | 146          | 78        |
| 9.      | PNB GILTS                   | 104 628           | 29        | NA           | 1         |
| 10.     | Hindalco Industries         | 82 549            | 3597      | 28           | 72        |
| 11.     | Coal India                  | 78 410            | 11 759    | 119          | 235       |
| 12.     | Bharti Airtel               | 71 506            | 6511      | 33           | 130       |
| 13.     | MMTC                        | 67 023            | 329       | 3            | 3         |
| 14.     | NTPC                        | 66 366            | 9334      | 49           | 187       |
| 15.     | Larsen & Toubro             | 64 960            | 4818      | 70           | 96        |
| 16.     | Essar Oil                   | 63 428            | -201      | NA           | N/A       |
| 17.     | Mahindra & Mahindra         | 63 030            | 2948      | 22           | 59        |
| 18.     | Mangalore Refinery & Petrochemicals | 57 214 | 1066 | NA           | 21        |
| 19.     | Tata Consultancy Services (TCS)| 48 894         | 8935      | 51           | 179       |
| 20.     | Bharat Heavy Electricals    | 50 654            | 5823      | 37           | 116       |

Total (100) | 1765 | 5611

Source: Jayashankar, M., Paul, C. & Bhat, S., 2013, ‘CSR report card: Where companies stand’, Forbes India, March 18, 2013.

Note: Companies are ranked on basis of revenue. Revenue figures are indicative of the company’s financial performance in financial year 2011–2012 (FY12) only. All figures are in Rs Crore and have been rounded off to the nearest decimal point. Avgas PAT refers to the average of profit after tax recorded by a company in the last three financial years (FY10, FY11 and FY12). NA stands for data ‘not available’ for companies which do not disclose their CSR spends in their annual reports. 2% of PAT refers to the amount that a company needs to spend in CSR activities as per the government mandate. N/A implies not applicable; according to government policy, loss-making firms do not need to invest in CSR.
has evolved substantially over the last few decades and is now witnessing unprecedented interest and investments across the value chain (PWC 2013). The corporates have responded positively to the reform measure undertaken by the government. The practice of CSR is not new to companies in India. However, this act brings more companies into the fold. Also, it is likely that the total CSR spending will increase. What is clear to many companies is that if this increased spending is to achieve results on the ground – which is the intent of the act – then it needs to be done strategically, systematically and thoughtfully (PWC 2013). The resulting flow of funding will position companies to help address India’s most pressing societal challenges. Equally exciting is how the corporate responsibility (CR) initiatives that companies launch will generate forms of value that matter to businesses. Examples include development of new sources of talent, improved infrastructure in the local communities where companies are operating and entry into new markets for innovative products or services developed for CR purposes. Businesses that can capture such value from their CR efforts and use it to drive new growth will play a major role in shaping India’s economic future (FICCI–Accenture 2014).

The India Survey suggests that many companies are already spending 2% or more on CSR as per the benchmark set in the Companies Act, 2013. However, experience in the space suggests that for many of these large corporations, this percentage figure becomes very large in absolute number and companies find it difficult to exhaust their budget stipulated for CSR activities completely if areas and methods of spending are restricted. India faces many challenges that require innovative ways of solving them, strengthening or creation of new institutions, research and debate, and on ground action (India Survey 2013). The CSR mandate could be an opportunity for corporates to move away from a narrow vision of CSR to a broader vision of corporate responsibility comprising actions that will help create a people- and planet-friendly business environment, enabling generation of socially responsible profits. An all-encompassing holistic view of corporate responsibility will usher in innovations, collaborations and organisational transitions that will make corporations commercially and socially viable in future (FICCI–Accenture 2014). Clearly, all this will involve considerable change – both within and outside a business’s walls. But the upfront investment will be well worth it. By adopting a disciplined approach to making the necessary changes, companies can make an unprecedented contribution to India’s future (FICCI–Accenture 2014).

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Competing interests

The authors declare that they have no financial or personal relationship(s) that may have inappropriately influenced them in writing this article.

Authors’ contributions

A.M. (University of Delhi) and A.J. (University of Delhi) contributed equally to the writing of this article.

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