An Analysis of CSR clause in the New Companies Act, 2013

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…………….Abstract……………….

This article attempts to analyze the differences between the Voluntary Guidelines on CSR, 2009 and the new Companies Act, 2012.It further tries to understand and define CSR in a more precise manner. This research is doctrinal in nature and throws light on why it was necessary for India to introduce CSR guidelines as an act, whereas it was just willful for many corporations till 2012. All the corporations have an undoubted obligation to use its resources in such a manner that it benefits the society, gives full committed participation as a member of the society and strive for the welfare of the society independently of the direct gains of the company.

The 21st century is characterized by unprecedented challenges and opportunities, due to the effect of globalization, the desire for inclusive development and the command of climate change. Indian corporations, which have been viewed globally as a responsible component of the ascendancy of India, is poised now to take on a leadership role in the challenges of our times. It is recognized the world over that environment, society and ethics are integral responsibilities into the governance of corporations so that they ensures their long term growth, success, competitiveness and sustainability. This approach also reassert the view that enterprises are an constituent part of society, and have an active evaluation and role to play in the sustenance and improvement of sustainable ecosystems, in nurturing social inclusiveness and equity, and in upholding the essentials of ethical practices and good governance. This also makes business sense as companies with effective CSR, have image of socially responsible companies, achieve sustainable growth in their operations in the long run and their products and services are selected or have an edge on the customers due to their goodwill in the market.

A new Companies Act has been in the pipeline for several years in India. The Companies Bill 2012 (the Bill) was finally passed on 18 December 2012 by the Lok Sabha. The Bill has metamorphosed several configurations of Voluntary guidelines, 2009 making it a law rather being just obligatory in nature. One such pertinent change is the introduction of a mandatory corporate social responsibility (CSR) investment of two per cent provided in Section 135.This paper includes the decoding some significant facts of the Voluntary guidelines and the new companies bill for easy understanding.

KEYWORDS: Voluntary Guidelines, CSR, Companies Bill, Clause 135, Globalization, Governance, Ethical Responsibility.

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"We have to choose between a global market driven only by calculations of short-term profit, and one which has human face. Between a world which condemns a quarter of the human race to starvation and squalor, and one which offers everyone at least a chance of prosperity, in a healthy environment. Between a selfish free-for-all in which we ignore the fate of the losers, and a future in which the strong and successful accept their responsibilities, showing global vision and leadership.

Kofi Annan, UN Secretary-General

January, 1999

Introduction:

Corporate Social Responsibility is largely a thought whereby corporations decide voluntarily to contribute to a much better society and a cleaner setting. Corporate social responsibility is delineated by the contributions undertaken by corporations to society through its business activities and its social investment. This is often conjointly to attach the construct of property development to the company's level.

Corporate Social Responsibility (CSR) can be understood as a management concept and a process that integrates social and environmental concerns in business operations and a company's interactions with the full range of its stakeholders.

Over the last years associate increasing range of corporations worldwide started promoting their company Social Responsibility ways as a result of the purchasers, the general public and also the investors expect them to act property still as accountable. In most cases CSR may be a result of a spread of social, environmental and economic pressures.

The Term Corporate Social Responsibility is imprecise and its application differs. CSR cannot solely talk over with the compliance of right standards, labor and Social Security arrangements, however additionally to the fight against global climate change, property management of natural resources and shopper protection.

The construct of Corporate Social Responsibility was first mentioned 1953 within the publication 'Social Responsibilities of the Businessman' by William J. Bowen. However, the term CSR became solely standard within the Nineteen Nineties, once the German Betapharm, a generic pharmacy determined to implement CSR. The generic market is characterized by associate interchangeableness of product. In 1997 a halt in sales growth junction rectifier the corporate to the conclusion that within the generic medicine market corporations couldn't differentiate on worth or quality. This was the prelude for the company to adopt CSR as associate expression of the company's values and as a section of its corporate methods. By victimization strategic and social commitment for families with inveterately sick youngsters, Betapharm took a strategic advantage.[1]

Concept and Growth of CSR: Globally and Nationally

[1] Global Compact (2008), Annual Review, 2008.

The rising conception of Corporate Social Responsibility (CSR) goes on the far side of charity and needs the corporate to act on the far side of its legal obligations and to integrated social, environmental and moral issues into company's business method.

Business has nowadays, emerged united of the foremost powerful establishments on the planet. A number of the most important firms within the world are real, larger in size than a number of the developing countries of the planet. Globalization makes the planet smaller, and business, worldwide, is increasing like never before. Firms' are increasing their operations and crossing geographical boundaries.

In the current scheme of things, business enterprises are no longer expected to play their traditional role of mere profit making enterprises. The ever-increasing role of civil society has started to put pressure on companies to act in an economically, socially and environmentally sustainable way.

Indian companies too have made their way into the business boom and are today globally acknowledged as major players. India is currently amongst the fastest growing countries in the world. The globalization and liberalization of the Indian economy has helped in stepping up growth rates. Integration of the Indian with the global economy has also resulted in Indian businesses opening up to international competition and thereby increasing their operations.

The companies are facing increased pressure for transparency and being accountable, being placed on them by their Stakeholders at large (employees, customers, shareholders, media, society, etc.). Firms does not operate in isolation and these days there's, an increased realization that not only can companies affect society at large, but they are also in a unique position to influence society and make affirmative impact.

Milton Friedman, Nobel Laureate in Economics and author of several books wrote in 1970 in the New York Times Magazine that "the social responsibility of business is to increase its profits" and "the business of business is business". This represented an extreme view that the only social responsibility a law-abiding business has is to maximize profits for the shareholders, which were considered the only stakeholders for the company. However, time has given the term 'stakeholder' wider connotations.[2]

Edward Freeman defines, 'a stakeholder in an organization is any group or individual who can affect or is affected by the achievement of the organization's objectives.' Thus, the term

Stakeholder includes (apart from shareholders), but not limited to, customers, employees, suppliers, community, environment and society at large.[3]

[2] http://www.indiacsr.in/en/?p=113
[3] Ibid

Certain **key elements of CSR** have been tried to explain and define by researchers so far by applying different methodological approaches: Some were summarizedby existing definitions (e.g. Carroll 1999; Moir 2001; Joyner and Payne 2002; Carter and Jennings 2004) , others were conducting interviews (e.g. O'Dwyer 2002; Johnston and Beatson 2005), analyzing research papers (e.g. Dahlsrud 2008; Montiel 2008; Taneja, Taneja et al. 2011) , or dealing with the development of a CSR definition through theoretical reasoning (e.g. Göbbels 2002; Van Marrewijk 2003; Matten and Crane 2005) . The following common characteristics can be seen as a list of key elements that are most commonly used:

- CSR is the liability of business to act in accordance to the overall goals of society, and is therefore linked to sustainable development as a guiding vision
- CSR depends on the political, institutional, and cultural context and environment, as it is dependent on the relationship between business and society
- CSR is beyond compliance: being compliant to laws or regulation are prerequisites of responsible corporate behavior.
- CSR is voluntary (otherwise it would be part of compliance), but it is still perceived as a moral, ethical, or philanthropic obligation of business. However, many NGOs and labor unions tend to question the idea of CSR as a voluntary concept.
- Making profits out of CSR: There is a lengthy debate on whether corporate measures that lead to profit can be perceived as CSR (e.g. "is it moral to make money out of being moral?") or – the other way round – if measures which do not lead to indirect profit at all, might be categorized as CSR (i.e. if philanthropy is part of CSR or not).

Summarizing these elements, CSR can be seen as a voluntary business contribution to the guiding societal model of sustainable development, and an active corporate engagement that goes beyond legal compliance (e.g. European Commission, 2001, European Commission, 2002).

CSR Framework:

In a Green Paper published in 2001, CSR was termed as a "concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with stakeholders on a voluntary basis (European Commission, 2001)." And in a Communication issued in 2002 it was said that "CSR is behavior by businesses over and above legal requirements, voluntarily adopted because businesses deem it to be in their long-term interest (European Commission, 2002)."

This definition has become a benchmark in Europe and a reference worldwide. The international framework for CSR continues to change via initiatives by international organizations including:

- The United Nations,
- The International Labour Organization,
- The Organization for Economic Cooperation and Development,
- The European Union.[4]

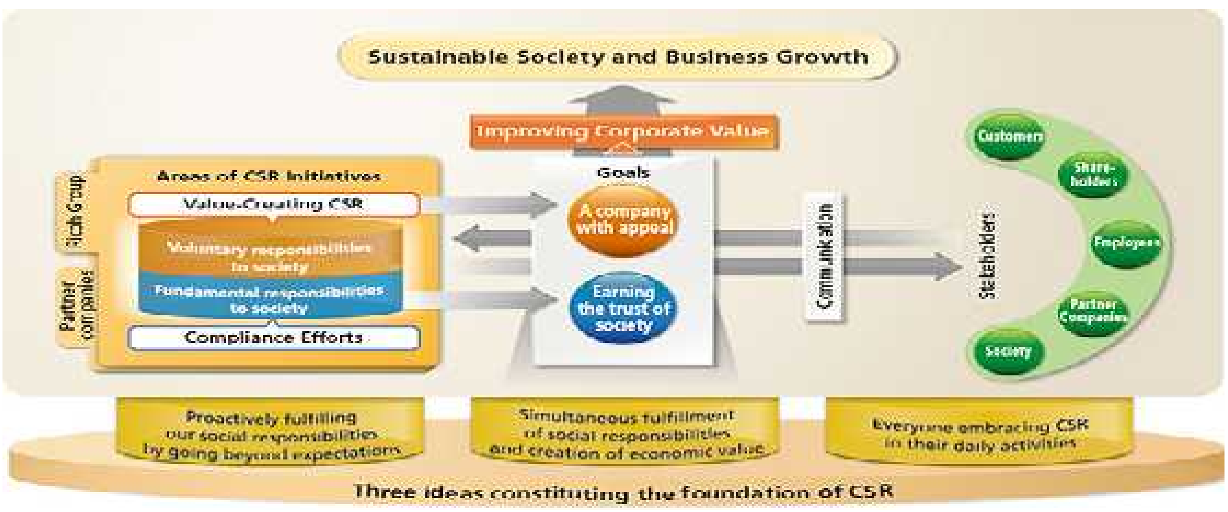

Fig. 1

Source: Ricoh Group Website

Voluntary Guidelines and Best Practices of CSR: India

The process of building up the Voluntary Guidelines started in the end of year 2009, by establishment of Guidelines Drafting Committee (GDC), which submitted its final recommendations of the draft NVGs to Ministry of Corporate Affairs (MCA) in November 2010.

[4] http://www.reportingcsr.org/international_csr_framework-p-7.html

The primary objective of these guidelines is to encourage adoption of sustainability reporting and mainstream disclosure on environmental, social and governance metrics. It is based on the premise that you can't change unless you measure. NVG provide businesses a framework which enables them to move towards responsible decision making and urges them to adopt the "triple bottom-line" approach.

In the year 2011, July the Ministry of Corporate Affairs, Government of India introduced the "National Voluntary Guidelines on Social, Environmental, and Economic Responsibilities of Business' – NVG's.

The NVG's talk about sustainability in companies through:

- Giving something back to the Society
- Be Responsible
- Be Accountable for the actions done by the organization, and
- Be sustainable in itself and in the environment it operates in.

There are many aspects of the society which are influenced by the organizations, such as given in the figure below:[5]

Fig. 2

The influence w.r.t. of an organization/company lies in the green shaded area where the important factors comprise Customers, Employees, Shareholders, etc. It is well known that the factors influence organization and vice-a-versa, but it is not these factors only which are important as the enterprise has implications on the larger areas of Economy, Policy, Community, Environment, etc.

[5] http://efficientcarbon.com/blog/introduction-to-national-voluntary-guidelines-business-responsibility-reporting

So, the need of the hour in organizations is, not only take the primary influencers into consideration but pay equal attention towards the broader areas too. The following advantages from the above process can be seen:

1) Ability to enhance competitive Skills

2) Enhancement OF Company and Brand Reputation

3) Ability to attract and retain good talent

4) Better management of Investors and Society

The NVG's work broadly on 9 principles which help enterprises to benefit and comply to requirements:

Fig. 3

Principle 1: Businesses should conduct and govern themselves with Ethics, Transparency and Accountability.

Principle 2: Businesses should provide goods &services that are safe and contribute to sustainability throughout their life cycle.

Principle 3: Businesses should promote the well being of all employees.

Principle 4: Businesses should respect the interests of, and be responsive towards all stakeholders, especially those who are disadvantaged, vulnerable and marginalized.

Principle 5: Businesses should respect and promote human rights.

Principle 6: Business should respect, protect, and make efforts to restore the environment.

Principle 7: Businesses, when engaged in influencing public and regulatory policy, should do so in a responsible manner.

Principle 8: Businesses should support inclusive growth and equitable development.

Principle 9: Businesses should engage with and provide value to their customers and consumers in a responsible manner.[6]

So, for all these principles companies need to provide with a declaration/report on their compliance and level of compliance by providing authentic numbers, data and specific cases relevant to each principle.

Reporting Process under NVG

The guidelines will be adopted by all firms regardless of their size or sector and area unit a singular, Indian version of a coverage framework that addresses the requirements of Indian stakeholders. Attributable to their universal pertinence, a special section has been enclosed within the draft NVG on the adoption of those tips by the resource unnatural small, tiny and medium enterprises (MSMEs) to alter larger future business opportunities and to assist them stay socially relevant.

NVG is versatile for corporations who square measure already following Associate in nursing internationally accepted property reportage framework. Such corporations aren't needed to publish a separate report, however will map the nine core principles of NVG to the disclosures created in their existing sustainability/business responsibility report. Corporations who have determined to adopt the NVG however don’t have the mandatory capability to furnish a full-fledged report will give an announcement of commitment to adoption of NVG to their stakeholders and furnish primary details on activities undertaken in respect to these pointers. Corporations who would really like to adopt NVG to the complete extent will furnish reports description their performance on environmental, social and governance factors supported the prompt framework.

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[6] http://www.mca.gov.in/Ministry/latestnews/National_Voluntary_Guidelines_2011_12jul2011.pdf

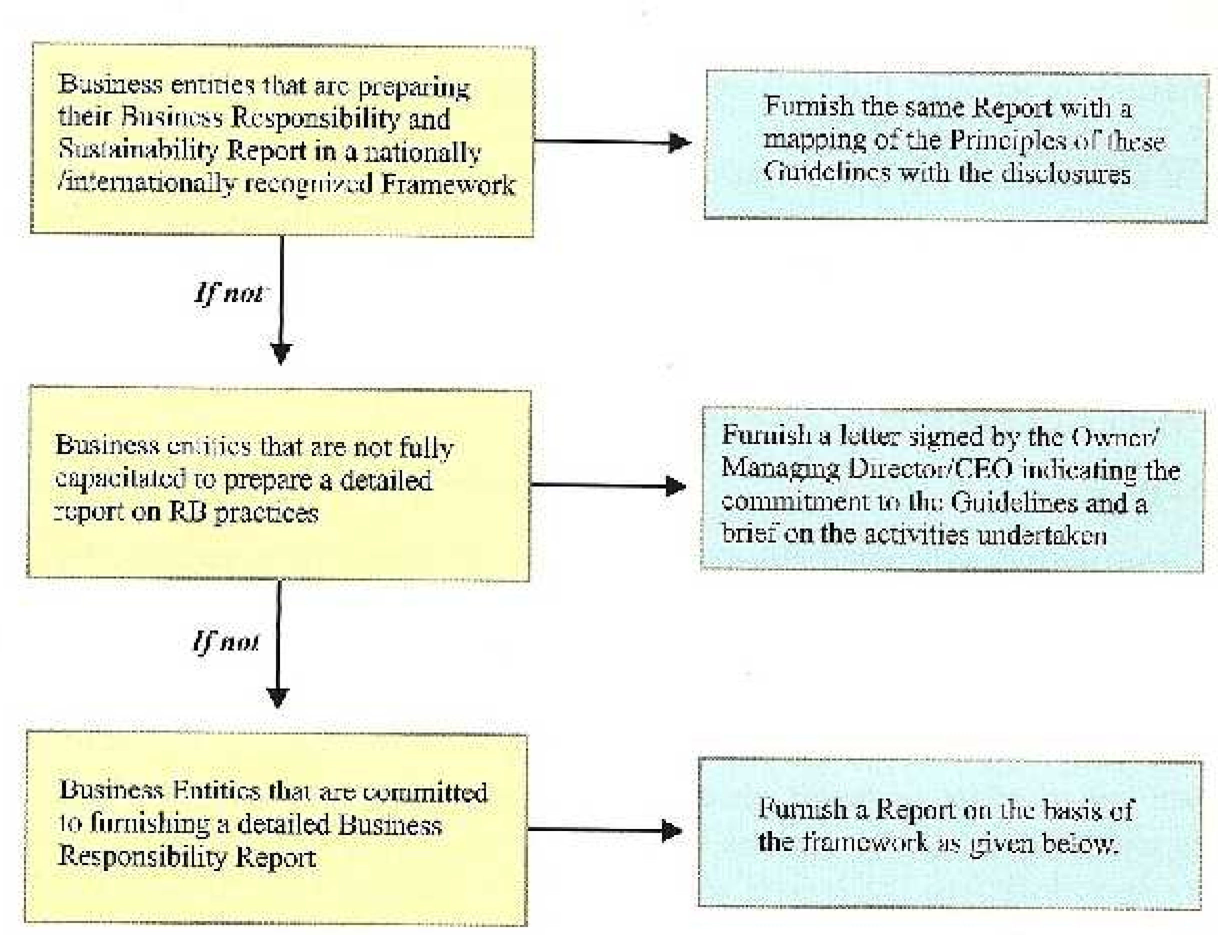

Fig. 4

Adherence to NVG guidelines by Indian Firms:

NVG, seemed to be a positive step in bringing about awareness around the need of taking into account both financial and non-financial metrics while assessing company's performance and it also helped in bringing speed laggards like India in the area of sustainability reporting. It can be seen that there is a tremendous shift in the mindset of companies – as, they have started seeing sustainability from the lens of opportunity instead of seeing it as a burden on the firm and in turn on their profit. The firm's are now able to realize the long term benefits associated with CSR and try to incorporate sustainability in their core business strategy. These guidelines gave given a concrete path and hence have improved to hasten the process.

CSR: Legislative Regulations

Global Scenario-

It can be observed that most of the countries worldwide have Social Responsibility guidelines which are not mandatory in nature but have legal implications if not adhered. As in the case of European Union's (EU) the new EU communication on CSR puts forward a replacement understanding of CSR, that now not refers to CSR as voluntary action on the far side compliance however highlights that each corporation causes impacts that is liable for. The impact areas (formerly simply society and environment) are enlarged by moral, human rights and shopper issues. To support policy learning among the EU Member States, the Commission invites member states to develop or update national CSR methods and action plans and sets up a referee system of public CSR policies. The maturity of public CSR policies differs among the EU member states significantly: two thirds of the EU member states have already got a CSR strategy and action arrange in situ or square measure presently developing such a policy document.

Danish government passed legislation in the year 2009, requiring 1,100 of the country's largest listed firms to include updates on CSR performance in their annual reports.Donald MacDonald, chair of the sustainable investment initiative the UN Principles for Responsible Investments, said there was a strong commercial case for businesses to embrace CSR and environmental reporting.

Similarly, Sweden was, in 2008, the first nation to impose CSR reporting obligations on state-owned companies, requiring companies to comply with the Global Reporting Initiative (GRI), a reporting framework that enables companies to measure and report their sustainability performance. Today, the second-highest number of GRI-based national reports in Europe can be attributed to Sweden.

Indian Trajectory-

As discussed above, CSR guidelines in India were voluntary in nature till the new Companies Act, 2013 came into being. The guidelines were based on the nine principles and had a reporting structure too. But, the new law could make Indian business simpler and more responsible as according to ***Doing Business* survey** The World Bank has placed India on the 132nd position out of 185 countries. The bill makes several sweeping changes in the way companies in India are defined, operated and are regulated. Most significantly, the new law is expected to bring greater transparency, free companies of excessive regulation and institute new ways of self-reporting and disclosure.

Many of the bill's options are debated, particularly the stipulation that corporations with a internet price of Rs. 500 crore ($100 million) or a lot of, or turnover of Rs 1,000 crore ($200 million) or a lot of, or a net income of Rs. 5 crore ($1 million) or a lot of throughout the past three monetary years should pay a minimum of a pair of 2% of their average internet profits from the three preceding years on CSR, or company social responsibility initiatives. Consistent with Union Minister of State for company Affairs Sachin Pilot, this stipulation makes India, the first Asian country within the world to de jure mandate company payment on financial aid.

The Companies Bill, 2013 has mentioned all the CSR guidelines under Clause 135, which are as follows:

- Every company having a net worth of rupees five hundred crore or more, or a turnover of rupees one thousand crore or more, or a net profit of rupees five crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.
- The Board's report under sub-section (3) of section 134 (o) shall disclose the composition of the Corporate Social Responsibility Committee.
- The Corporate Social Responsibility Committee shall,
- formulate and recommend to the Board, a Corporate Social Responsibility Policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII;
- recommend the amount of expenditure to be incurred on the activities referred to in clause (a); and
- monitor the Corporate Social Responsibility Policy of the company from time to time.

- The Board of every company referred to in sub-section (1) shall,
  - After taking into account the recommendations made by the Corporate Social Responsibility Committee, approve the Corporate Social Responsibility Policy for the company and disclose the contents of such Policy in its report and also place it on the company's website, if any, in such manner as may be prescribed; and
  - ensure that the activities as are included in Corporate Social Responsibility Policy of the company are undertaken by the company.
- The Board of every company referred to in sub-section (1), shall make every endeavor to ensure that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy;

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

The Clause also states those activities, which can be undertaken as CSR activities by organizations:

i. ***eradicating extreme hunger and poverty;***
ii. ***promotion of education;***
iii. ***promoting gender equality and empowering women;***
iv. ***reducing child mortality and improving maternal health;***
v. ***combating human immunodeficiency virus, acquired immune deficiency*** **syndrome, malaria and other diseases;**
vi. ***ensuring environmental sustainability;***
vii. ***employment enhancing vocational skills;***
viii. ***social business projects;***
ix. ***contribution to the Prime Minister's National Relief Fund or any other*** **fund set up by the Central Government or the State Governments for socioeconomic development and relief and funds for the welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women; and**
x. ***such other matters as may be prescribed.***[7]

There have been mixed reactions to the introduction of the 'spend or explain' approach taken by the MCA with respect to CSR. It may take a while before all of Corporate India imbibes CSR as a culture.

Clause (o) of Sub-Section (3) of Section 134

There shall be attached to statements laid before a company in a general meeting, a report by its Board of Directors, which shall include:

- The details about the policy developed and implemented by the company on corporate social responsibility initiatives taken during the year.
- If a company contravenes the provisions of this section, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

[7] www.mca.gov.in/Ministry/pdf/**Companies**Act**2013**.pdf

Unanswered Questions:

However, activities specified in the Schedule are not elaborate or detailed enough to indicate the kind of projects that could be undertaken, for example, environment sustainability or social business projects could encompass a wide range of activities.

The committee will also need to recommend the amount of expenditure to be incurred and monitor the policy from a time-to-time. The board shall disclose the contents of the policy in its report, and place it on the website, if any, of the company. The 2013 Act mandates that these companies would be required to spend at least 2% of the average net-profits of the immediately preceding three years on CSR activities, and if not spent, explanation for the reasons thereof would need to be given in the director's report (section 135 of the 2013 Act).

Critical Appraisal/Conclusion:

1. Is it better to have CSR voluntary, so as to give liberty to each organization to adjust it accordingly to its capacity and location, while law (Companies Bill, 2013) is rigid and not flexible
2. Compulsory CSR is to be applied to specific programs (which are given under Section 135 of Companies Law 135) hence no other program will fall under it. It is therefore limited and may not help the Stakeholders of CSR while voluntary one's can be diverted to specific group stakeholders depending on the need of the time and place.
3. Practice of Voluntary CSR should have been continued along with compulsory CSR as supplementary. The removal of voluntary guidelines by the compulsory one is bound to produce gap, thus, hamper economic development and in turn the National growth.