ISAS Insights

No. 121 – 6 April 2011

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Political Economy of CSR: The Companies Bill Debate in India

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Abstract

The concept of 'Corporate Social Responsibility' (CSR) is not new to the Indian corporate world. The recent proposal by India's Ministry of Corporate Affairs (MCA) to make philanthropy compulsory by law under the Companies Bill 2009, however, gave rise to a raging debate in the country. Many questions were raised including whether a rule-based approach to philanthropy is needed and whether making CSR spend mandatory by law would yield the desired outcomes? However, before one answers these questions, it is important to reflect on one fundamental aspect under the CSR debate. If socially responsible behaviour has become key to corporate agendas, then why have only some firms behaved in a socially responsible manner while others have not? This paper examines the factors that govern such behaviour on the part of firms and traces its relevance to the current CSR debate in India.

Introduction

CSR has assumed an integral role as a corporate philosophy the world over. In India, it has given rise to a raging public debate in recent times. In a bid to bridge the gap between CSR initiatives on the part of India Inc., the MCA decided to mandate corporations to set aside a part of their earnings towards CSR under the Companies Bill 2009. However, fierce

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opposition by firms against mandatory CSR has led the MCA to reconsider the provision and it seems to be unlikely that it is made compulsory, even though the guidelines will remain in the Bill.[2] Marred by such debates, the Bill is now expected to be introduced in the Monsoon Session (July 2011) of the Parliament since it had missed the deadline for the recently concluded Budget Session (February to March 2011) as had been announced by the Finance Minister Pranab Mukherjee at the start of the Budget Session.[3]

The existing Companies Act of 1956 has no specific provisions towards CSR and the MCA hopes to amend the situation by way of the Companies Bill 2009 that aims to replace the half-a-century-old Act. With this in mind, the Parliamentary Standing Committee on Finance (PSCF), headed by former Finance Minister Yashwant Sinha, had suggested a provision of a mandatory CSR spend on companies meeting specified financial criteria. Building upon the suggestion, the MCA had announced that 'every company having [net worth of US$1 billion or more or alternately a turnover of US$2 billion or more] or [a net profit of US$1 million or more during a year] shall be required to formulate a CSR policy as may be approved and specified by the company by MCA standards.'[4]

Under the initial draft provisions of the Bill, private sector units are expected to contribute between two to five per cent of their profits depending on their earnings. For public sector units, this expenditure has been capped between 0.5 and 2.0 per cent of their net profit. The Government, however, has accepted that industries should be allowed to monitor the implementation of CSR without intervention. Also, the MCA is currently weighing if there is room for a statutory requirement. India Inc. has expressed concerns that a compulsory spend would give rise to malpractice.[5] Further, while most developed economies have provisions on CSR, there are hardly any jurisdictions mandating this form of responsibility levy, an argument cited by India Inc.

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2 Ronojoy Banerjee, *The Financial Express* (22 February 2011), www.financialexpress.com/news/india-inc-slams-making-csr-spend-mandatory/753034/0. Accessed on 28 March 2011; Mahua Venkatesh, 'CSR spending to be voluntary, not mandatory, under new law', *Hindustan Times* (13 March 2011), www.hindustantimes.com/CSR-spending-to-be-voluntary-not-mandatory-under-new-law/Article1-673041.aspx. Accessed on 14 March 2011.

3 'Companies Bill to be presented this Budget session: FM' *The Indian Express* (28 February 2011), www.indianexpress.com/news/companies-bill-to-be-presented-this-budget-session-fm/755850/. Accessed on 28 March 2011; 'Government to consult corporates on 2% profit for CSR activities: Singh', *ASSOCHAM* (11 March 2011), www.assocham.org/prels/shownews.php?id=2795. Accessed on 28 March 2011; Souvik Sanyal & Rajeev Jayaswal, 'Draft cos bill grants govt power to block multiple-layer setups,' *The Economic Times* (14 March 2011), http://articles.economictimes.indiatimes.com/2011-03-14/news/28688238_1_subsidiaries-corporate-affairs-law-ministry. Accessed on 16 March 2011.

4 Ronojoy Banerjee, 'India Inc. Slams Making CSR Spend Mandatory', *The Financial Express* (22 February 2011), www.financialexpress.com/news/india-inc-slams-making-csr-spend-mandatory/753034/0. Accessed on 12 March 2011.

5 Mahua Venkatesh, 'CSR spending to be voluntary, not mandatory, under new law', *Hindustan Times* (13 March 2011), www.hindustantimes.com/CSR-spending-to-be-voluntary-not-mandatory-under-new-law/Article1-673041.aspx. Accessed on 16 March 2011.

According to Capitaline data, over ₹4,300 crore (approximately US$960.6 million) would have to be set aside by corporate entities for CSR during the fiscal year, if the provisions regarding a CSR levy are put to effect.[6] Further, considerations under the CSR clause include mandatory disclosure to shareholders about the policy adopted in the process. The MCA is also considering introducing different provisions for listed as well as unlisted companies as it feels that the two types of organisational structuring have different requirements.

With the CSR issue looming large over India, what is puzzling (in the more generic debate around the idea of CSR) is that if socially responsible behaviour is such a norm of the day, then why do only some firms behave in a socially responsible manner while others do not? Only a handful of names emerge when studies regarding CSR initiatives are published while others have either 'simply failed to pay much attention' or 'think they can afford to ignore CSR'.[7] This paper explores the concept of CSR, highlighting the causes for lack of voluntary CSR initiatives in corporate philosophy globally and ties it to the current debate around the CSR provision according to the Companies Bill in India.

CSR and Philanthropy

The concept of CSR has bloomed over the past decade, and following the 2002 Johannesburg World Summit on Sustainable Development organised by the United Nations, phrases such as socially responsible investment and sustainable development have gained currency, and now warrant much attention from the globalised world.[8] While there is still much contention over a standard definition, *The Economist*'s view that CSR is 'the tribute that capitalism everywhere pays for virtue', and it now exists as 'an industry in its own right',[9] may provide the context for examining the field. The concept of CSR is now moving towards the premise that firms can be successful in serving the interests of its shareholders even as they serve the larger purpose of being socially responsible and as *The Economist* notes, 'doing well by doing good' is quickly being engrained in corporate philosophy. That said, only some companies have chosen to embrace CSR while others have restricted to peripheral initiatives under the CSR umbrella.

This contrast of socially responsible behaviour by firms, to a large extent, is governed or influenced by certain factors that can be categorised under economic and institutional factors. The variations in primary economic considerations such as economic environment, financial performance and a level of competition, among others, govern the motivation of firms to devise ways that reflect social responsibility. Such decisions are also affected by the diversity

6 'India Inc faces 2% CSR levy', *Business Standard* (8 September 2010), www.business-standard.com/india/news/india-inc-faces-2-csr-levy/407350/. Accessed on 16 March 2011.
7 'The Good Company', *The Economist* (22 January 2005), p.22.
8 For details on the summit see, www.un.org/jsummit/html/basic_info/basicinfo.html. Accessed on 28 March 2011.
9 'The Good Company', *The Economist* (22 January 2005), p.3.

in institutional factors, which include the role of government regulations and monitoring, non-government organisations (NGO), media organisations and other civil society groups, and some contemporary factors such as emergence of managers who have been trained to operate in socially responsible ways via their socially relevant curricula at business schools and similar institutions.

Economic Conditions and Factors

The relative health of an economy, along with the economic health of the firm itself, creates conditions for the firm to behave in a socially sensitive manner. Firms with weak financial performance are less likely to engage in socially responsible behaviour than those with stronger financial grounding. The primary reason for this notion is that, a less financially stable firm would find it difficult to spare any resources for CSR activities while a financially well-off company can easily devote a noticeable share of its resources to CSR. Thus, it is not surprising that most of the firms that are diligent CSR practitioners are the ones with biggest market capitalisation such as Shell and General Electric (GE). Further, one can also argue that if the economic environment is not conducive for reaping profits (eg. the global financial crisis and subsequent recession), the chances of firms investing behind CSR is also diminished since they cannot afford to further risk any losses in shareholder investment and would be less inclined in some cases to even meet the minimum standards of socially responsible behaviour.

The level of competition that a firm faces vis-à-vis other firms, is another factor that can influence a company's need to carve a CSR agenda. If this belief holds true, then a company's inclination to be socially responsible may also be governed by its competitors and the level of competition it faces. In cases where firms face intense competition, there is an added pressure to sustain bottom lines and profit margins and thus, there is a need to cut down on all additional expenses. Hence, philanthropy is likely to take a back seat and may even push firms into socially irresponsible acts, such as reducing jobs and incentives or increasing working hours, in a bid to survive. Furthermore, firms from developing countries may not have adopted CSR practices since they need to devote their resources to setting up business and subsequently compete with established brands, before they can inculcate the social responsibility habit. This problem, however, may be restricted to developing countries and their homegrown firms. In India, however, there has been an increasing shift in favour of CSR both by domestic as well as foreign players and is especially visible in the fast moving consumer goods (FMCG) sector, where firms seem to be competing not only in the traditional market place but also on the CSR turf.

For some firms, the obligation to maximise profits and interests of its shareholders may prevent it from acting in a socially responsible manner as 'their job is to make money for shareholders' and 'it is irresponsible for them to sacrifice profits in the (sometimes vain) pursuit of goodness'.[10] Therefore, it is not surprising that executives of firms such as British retailer Marks and Spencer, while formulating socially relevant actions such as its environment-oriented 'Plan A', bear in mind that their firm is a business and not a green charity.[11] Further, claims such as 'corporate philanthropy is charity with other people's money, which is not philanthropy at all,' make some firms wary of the concept of CSR itself.[12]

The motivation for CSR may especially be strong for firms involved in what may be described as socially objectionable businesses such as tobacco and alcohol. Often, such firms try to gain the trust of consumers and civil society by trying to cover the negative business aspects under the CSR umbrella. For example, companies like British American Tobacco (BAT) and even McDonald's have indulged in distracting the public eye from their core business. For other firms that have not been criticised yet for their field of work, CSR assumes the role of a risk management exercise.[13] Oil and mining firms, involved in high risk businesses are likely to have stronger CSR programmes to mitigate the risk of reputation in crisis. The bad press that followed Nike for years after its infamous sweat shop and human rights controversy compelled it to champion the cause of CSR. A more recent example is that of Deepwater Horizon Oil Spill of 2010 in the Gulf of Mexico, which brought much public ire to British Petroleum (BP) besides the plethora of lawsuits that tainted the company's name.

However, the desire to be socially responsible has been increasingly finding favour with big and small firms alike. This is because of a growing need for firms to preserve their reputation, maintain an edge over competitors and ensure business flow, even in times of crisis. Going by the experiences of Enron, BP and Nike among others, it has become pertinent for firms to cultivate loyal consumers who are increasingly in favour of socially responsible brands. This can be understood by the 'towel experiment' wherein Michael Hiscox and Nicholas Smyth noted that the towels with a label of 'Fair and Square' conveying fair labour conditions during manufacturing sold more than the ones without any labels, indicating a shift in consumer mindset.[14]

Another situation wherein firms may not want any socially responsible involvement can be in the cases of monopoly or lack of competition. Such a situation, though largely diminishing, may be observed in some state-owned firms or in a protectionist trade environment and thus may not warrant any socially responsible behaviour.

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[10] 'Just Good Business', *The Economist* (19 January 2008), p.9.

[11] *Ibid*. Marks and Spencer's 'Plan A' is about working with customers and suppliers to combat climate change, reduce waste, use sustainable raw materials, trade ethically, and help customers to lead healthier lifestyles. More details can be found at http://plana.marksandspencer.com/about. Accessed on 28 March 2011.

[12] 'The Union of Concerned Executives: A Survey on Corporate Social Responsibility', *The Economist (*22 January 2005), p.8.

[13] For details see, 'A Stitch in Time: in Just Good Business', *The Economist* (19 January 2008), p.10.

[14] *Ibid*., p.14.

Institutional Factors

A common institutional factor that has pushed firms to act responsibly is the role of governments themselves. Governments can ensure an atmosphere of sustainable development by implementing regulations that induce responsible behaviour in corporate organisations. *The Economist* has pointed out that firms as diverse as the pharmaceutical company GlaxoSmithKline, retailer Walmart and sporting goods brand Nike have amended their ways to prevent any regulatory backlashes.[15] India's own MCA, too, seems to be following suit and hence feels the need to add the CSR clause in the Companies Bill. However, a counter argument for this would be that CSR is still a voluntary act and firms left to their own devices can choose not to comply with the guidelines.

However, regulations alone cannot ensure informed acts on the part of firms, governments also need to monitor these firms and their actions. The 2006 Companies Act in Britain, which introduced a requirement for public companies to compulsorily disclose on matters such as social and environmental issues, is an attempt by the British government to ensure better CSR.[16] In a first, the MCA in India also put up a set of voluntary guidelines on CSR to elicit response and grow the concept. These guidelines have identified core elements such as care for all stakeholders, ethical functioning, respect for workers' rights and welfare, respect for human rights, respect for environment, and activities for social and inclusive development. The mandatory CSR provision seems to be the next step in this progression by the MCA.[17]

Among other success stories, the Mercados Verdes programme in Colombia is viewed as a pioneering example of public sector support for sustainable markets in Latin America.[18] The programme has been designed to incentivise production of environmentally-friendly goods and services that are competitive in international markets. In Peru, the responsibilities of Pro Inversion, the private investment promotion agency, include the following – 'To attract investors able to transfer state-of-the-art technology and to take responsibilities with respect to the development of their social environment' and 'To assist in the disclosure, among potential investors, of the role and social commitment they have with the environment and people'.[19] The goal of the agency's work is expressed as being: 'to foster competitiveness and sustainable development in Peru to improve the welfare of the Peruvian people'.

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15 'How Good should your Business Be?' *The Economist* (19 January 2008), p.13.

16 'Just Good Business', *The Economist (19* January 2008), p.13.

17 For details of the Voluntary Guidelines see, Ministry of Corporate Affairs, India website: http://mca.gov.in/Ministry/latestnews/CSR_Voluntary_Guidelines_24dec2009.pdf. Accessed on 28 March 2011.

18 United Nations Department of Economic and Social Affairs, 'CSR and Developing Countries: What Scope for Government Action?', *Sustainable Development Innovation Briefs*, Issue 1 (February 2007), p.3, www.un.org/esa/sustdev/publications/innovationbriefs/no1.pdf. Accessed on 20 March 2011.

19 *Ibid.*, p.4

Another institutional factor that proves decisive in a firm's quest for CSR is the presence of strong monitoring mechanisms such as the media, NGOs and the civil society at large. Slightest misbehavior on the part of corporate is met by much ire by the ever-increasing scrutiny net of civil society watchdogs. The media plays a great role in highlighting the social incompetence of firms, costing a big dent in the brand value of these firms. In India, the pesticides controversy had caused the sales of Coca-Cola and PepsiCo products to fall drastically.[20]

Employee satisfaction is another element that can be added to the CSR debate wherein by adopting CSR initiatives firms can strengthen ties with their workers. GE's 'ecomagination' initiative promoting green technology has struck a chord with consumers and employees alike so much so that employees have contributed new ideas that are worth around US$70 million per annum in energy savings. It has also helped instill a sense of trust in the environmentalist who picked on the company for dumping toxic waste into the Hudson River years ago.[21] Further, the role of institutions such as business schools have also come to play a significant role in preparing managers who strive to make the right business decisions while incorporating a CSR vision.[22]

Some Considerations

The preceding section tried to highlight some of the key reasons for a lag in CSR initiatives by firms globally and the case in India is not very different.[23] The CSR debate across the globe has now moved beyond blind donations and mere responsibility towards employees. It now entails a conscious incorporation of larger issues such as saving the planet and getting involved. Harvard University's John Ruggie rightly points out, 'The theological question – should there be CSR? – is so irrelevant today.'[24]

Policymakers in India should consider certain factors before finalising the CSR diktat under the Companies Bill. First and foremost, there is a dire need to arrive at a clear definition of CSR and what it entails in the Indian context. A general lack of consensus over a standard has dogged the international debates on CSR and it is essential to get this right before proceeding onto the next step. In tandem with this, the MCA also needs to identify and engage the stakeholders while formulating policies around CSR. Since CSR should be applicable to all companies regardless of their size and sector, the MCA should aim to level the playing field

[20] Amelia Gentleman, 'Pesticide allegations trip up Coke and Pepsi', *The New York Times* (22 September 2008), www.nytimes.com/2006/08/22/business/worldbusiness/22iht-coke.2562750.html. Accessed on 17 March 2011.
[21] For details see, 'Just Good Business', *The Economist,* (19 January 2008), p.16.
[22] *Ibid*., p.4.
[23] The list of factors cited in this paper is not exhaustive.
[24] John Ruggie is also the United Nations Special Representative of the Secretary General on human rights and transnational corporations and other business enterprises.

keeping in mind that each industry works under different sets of constraints. It is essential to try and accommodate the stakeholders as far as possible in order to make CSR more effective.

Second, CSR agendas in middle and low income countries have traditionally been less visible internationally and at times have not been recognised as and granted a 'CSR label'.[25] In this context it is important that the Government does not set the national CSR agenda just to gain acceptance by international watchdogs and not to promote socially responsible practices by businesses. That said, internationalisation of standards and adoption of CSR codes and standards such as ISO 14001 and the Global Reporting Initiative's Sustainability Reporting Guidelines warrant a proactive response on the part of India Inc. to remain globally competitive even on the CSR front. The Government can play a fundamental role in imparting education and assisting small and medium enterprises (SMEs) in responding to these global demands instead of formulating a law and leaving small businesses to their own devices.

Third, a compulsory CSR provision would entail a long process of legislations, and a series of allied legislations would also be required to ensure the desired end-use. This, in turn, would require dozen-odd legal provisions to protect such legislation and resources. As Biocon Chairman and Managing Director, Kiran Mazumdar, noted, '…would make the process very cosmetic'. For India, which has been dogged by a series of money laundering and similar scams, a CSR mandate by law could add to yet another avenue of fraud and illegality. Wipro Chairman Azim Premji too expressed his concerns recently, 'My concern is that you get legislation ... and a lot of abuse takes place from that legislation in terms of what you define as CSR and what you define as branding. I would be against it.'[26] Another consideration in this regard is whether charity by force can actually yield to desired outcomes? This is an important consideration in the context of the CSR debate in India. Being socially responsible ultimately is a matter of willingness and an attitude of philanthropy cannot be mandated.

Fourth, India's CSR story can be successful only if companies could view CSR from their own perspective as a part of business strategy that also benefits the community. A goal based approach rather than a diktat-based approach could incentivise firms to adopt CSR. For example, Mexican Environmental Protection Agency's (PROFEPA) Industria Limpia programme, which is based on firm-specific negotiated agreements towards plant-based

[25] United Nations Department of Economic and Social Affairs, 'CSR and Developing Countries: What Scope for Government Action?', *Sustainable Development Innovation Briefs*, Issue 1, (February 2007), www.un.org/esa/sustdev/publications/innovationbriefs/no1.pdf . Accessed on 20 March 2011.

[26] Press Trust of India, 'Azim Premji against law on mandatory CSR spending by corporates,' *The Economic Times* (24 March 2011), http://economictimes.indiatimes.com/news/news-by-company/corporate-trends/premji-against-law-on-mandatory-csr-spending-by-corporates/articleshow/7782555.cms. Accessed on 24 March 2011.

environmental improvements along with a certification and labelling scheme.[27] The programme is designed to attract the 'leader' firms in CSR to show leadership by example.

Conclusion

While there is still no concrete proof that more responsible firms are more profitable, it is also not evident that less socially responsible ones are not. The challenge then is to balance the scales between profit and sustainable development in the long run as has been recognised by firms such as Walmart and Mars.[28]In India too, the trend is emerging. For example, Reliance Industries Limited Chairman Mukesh Ambani, who is also the richest Indian, feels that CSR needs to evolve into Continuous Social Business. 'The purpose of any business cannot be only profit. Profit for the shareholders is important. But unless entrepreneurs have a larger purpose and businesses that change lives of millions of people, a sustainable business cannot be created.' [29]

Further, the proposed CSR provisions in India also include the Public Advisory Committee of the Institute of Chartered Accountants of India (ICAI) that has been set up with a view to protect public interest. ICAI will advise companies to take up CSR projects specific to the industry they belong to. Companies in the chemical industry for example, would be advised to take up projects relating to environmental protection according to them. The ICAI will also chalk out plans for a new accounting system to keep a record of all company spends on CSR. Such guidance perhaps is a better approach than mandating a compulsory spend.

World's leading philanthropists – Warren Buffet and Bill Gates –visited India in March this year in a bid to persuade billionaires to pledge at least half their fortunes under the 'Giving Pledge' programme.[30] This may well be an indicator of how India Inc. is already doing or is geared to do its bit when it comes to CSR and a law may perhaps not be required. Mathew Bishop and Michael Green in their book, 'Philanthrocapitalism: How Giving Can Save the World', have made a case for India's rise up the philanthropy table and sides Bill Gates' belief that, 'India could soon be the world's second most philanthropic nation, after America.'[31] This optimism around India and its philanthropic spirit is perhaps well founded.

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[27] United Nations Department of Economic and Social Affairs, 'CSR and Developing Countries. What Scope for Government Action?', *Sustainable Development Innovation Briefs*, Issue 1 (February 2007), www.un.org/esa/sustdev/publications/innovationbriefs/no1.pdf . Accessed on 20 March 2011.

[28] Michael Skapinker, 'Why Corporate Responsibility is a Survivor', *The Financial Times* (20 April 2009).

[29] Press Trust of India, 'Not just CSR but Continuous Social Business need of the hour: Mukesh Ambani', *The Economic Times* (1 March 2011), http://articles.economictimes.indiatimes.com/2011-03-01/news/28645671_1_mukesh-ambani-csr-corporate-social-responsibility. Accessed on 17 March 2011.

[30] Dow Jones Newswires, 'Buffett Looks Beyond Home Turf To India For Invest Opportunities', *The Wall Street Journal* (22 March 2011), http://online.wsj.com/article/BT-CO-20110322-711288.html. Accessed on 22 March 2011.

[31] Mathew Bishop, 'Philanthrocapitalists Needed in India', *Mint* (17 March 2011), www.livemint.com/2011/03/17221001/Philanthrocapitalists-needed-i.html?h=B. Accessed on 18 March 2011.

Delegated legislation may become indispensible in the wake of future issues such as environmental pressures, impact of global operations of Indian firms on domestic stakeholders and technological collaborations, among others. However, corporates need to first develop and embrace CSR at an individual level. Efforts such as developing internal monitoring systems to gauge quality and the reach of their performance can prepare corporates for a rule-based approach to socially responsible behaviour.

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