A study on implications of Corporate Social Responsibility under Companies Act, 2013

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Abstract: Corporate social responsibility (CSR) is a business approach that contributes to sustainable development by delivering economic, social and environmental benefits for all stakeholders. The way it is understood and implemented differs greatly for each company and country. Moreover, CSR is a very broad concept that addresses many and various topics such as human rights, corporate governance, health and safety, environmental effects, working conditions and contribution to economic development. The purpose of CSR is to drive change towards sustainability. CSR or citizenship aims at invoking the corporate conscience whereby companies incur short-term costs that do not provide an immediate financial benefit to them, but instead promote positive social and environmental change. The New Companies Act 2013 has come up with the concept of mandatory CSR and this Act replaces the archaic, almost 60 yrs old Companies Act, 1956. This paper is focused on Companies Act, 2013 & its provision on mandatory spending and disclosure of Corporate Social Responsibility activities. The paper also discusses the major loopholes in the provision that can prove as a hindrance in its practical applicability.

INTRODUCTION

In recent years there has been significant awareness and interest about a firm’s Corporate Social Responsibility (CSR) initiatives and its financial performance. CSR does not only mean to donate to the victims of natural calamities or to pay dividend to the Govt. exchequer or to comply with the provisions of national legislations. CSR has generally centered on voluntary actions, policies and practices undertaken by firms that are related to the firm’s business ethics, community involvement and investment, social and environmental concerns/sustainability, human relations/right-especially its treatment of its employees and overall business practices. Creation of facilities and infrastructure for the common people and to ensure their sustainability are more important responsibility agenda of the corporate sector for a country like India where a substantial portion of people are living below poverty line. CSR is closely linked with the principles of “Sustainable Development” in proposing that enterprises should be obliged to make decisions based not only on the financial/economic factors but also on the social and environmental consequences of their activities.

STATEMENT OF THE PROBLEM

Over the last three decades, India has undergone a process of economic liberalization and is amongst the fastest growing economies in the world. The Industrial sector has been able to create abundant wealth over the years. Yet, the growth has not trickled down to the masses leaving a large proportion of population with limited access to basic amenities such as clean sanitation, clean water, health facilities etc. The uneven distribution of income can be the root cause of social unrest. As rich continues to get richer and poverty statistics not improving, the government has sought to bring the corporate sector into the picture as an important contributor to social development activities. The Indian state has also made bold steps to help channel the economic successes of business to those who need it most. With introduction of corporate social responsibility (CSR) guidelines under the New Company’s act it became the first country to have CSR legislation. The government has mandated corporations over a certain net worth to spend two percent of their last three years’ average net profit on social development, report on the activities or explain in case they failed to spend. The CSR clause within the Companies Act, 2013 seems to be an honest attempt to achieve the goals of equitable development and at the same time promoting greater transparency and disclosure. How long India takes to redefine the concept and how corporate India moves away from philanthropy to a world of redistribution of wealth are important issues.

LITERATURE REVIEW

Oil India Limited conducted a social survey in its operational areas in the North-East through Dibrugarh University to evolve a CSR strategy in the year 1983. Based on the recommendation of the survey, the company introduced a scheme called “Social Welfare Programme” (SWP) in 1984 and in the year 1996, it introduced another scheme called “Area Development Scheme” (ADS).

As summarized by Business for Social Responsibility, a 1999 study conducted by Environics International Ltd., The Prince of Wales Business Leaders Forum, and The Conference Board Surveyed 25000 citizens in 23 countries regarding corporate social responsibility. The highlights of the findings included the following:

Ninety percent of respondents want companies to focus on more than profitability.

- Sixty percent said they form an impression of a company based on perceptions of social responsibility.
- Forty percent said they either responded negatively to or said negative things about companies they perceive as not being socially responsible.
- Seventeen percent reported they had actually avoided the products of companies if they perceived them as not being socially responsible.
- Mobile dispensary program ranked as one of the most “useful” OIL initiatives.
• Self-Help Group (SHG) Scheme of OIL and SIRD (State Institute of Rural Development) is the current ‘favourite’.

• Schools, colleges or cultural centers drew high community involvement.

According to K.P.M.G., a U.S. Professional services firm, a 2002 survey of the Global Fortune Top 250 companies indicated a continued increase in the number of American companies reporting on corporate responsibility. In 2002, 45% of these companies issued environmental, social or sustainability reports, compared with 35% in their 1999 survey.

In 2004-2005, Oil India Limited conducted a Social audit of its CSR initiatives. M/S Enterprise Group, New Delhi, a professional agency was engaged to carry out the audit to assess the impact and public participation of the same. The key findings of the audit were:

From the survey of literature the following conclusions can be made:

• The relationship between financial performance and social responsibility is not firmly established but profit is perceived as a precondition and it is one of the most important goals of business.

• There is an increasing awareness and acceptance of social responsibility in today’s business environment. In fact up to 100% of all Fortune 500 companies engage in Corporate Social Responsibility initiatives. It includes: equal employment opportunities, philanthropy, pollution control, community development etc.

• Research in business-society field is increasing quantitatively as well as qualitatively. Growing interest in the field among scholars and efforts of the analysts of prominent business are responsible for this outcome.

• Social auditing is helpful to identify social issues, evaluate performance and to inject social view into the thinking of managers. But, it suffers from the lack of acceptable measures for making proper evaluation.

• High Level Management is primarily responsible for initiation and successful implementation of social welfare programmes.

Objectives of the study:

1. To study the CSR statute in India
2. To highlight the provisions of New Companies Act related to CSR mandate
3. To study the key areas in the current CSR legislation which can be a hindrance for applicability of the CSR legislation.

Research Methodology:

The research paper is an attempt of exploratory research, based on the secondary data sources. Looking into requirements of the objectives of the study the research design employed for the study is of descriptive type. Available secondary data was extensively used for the study.

Provisions of CSR under New Company’s Act: 2013:

Under Section 135(5) of the new Companies Act, 2013, passed by Parliament in August 2013, profitable companies must spend every year at least 2 per cent of their average net profit over the preceding three years on CSR works and shall not include profits arising from branches outside India. This mandatory CSR-spend rule will apply from fiscal 2014-15 onwards. CSR, which has largely been voluntary contribution, by corporate has now been included in law. Tax treatment of CSR spend will be in accordance with the IT Act as may be notified by Central Board of Direct Taxes (CBDT). Section 135 of the 2013 Act states that every company having Net worth of Rs 500 crore or more, or Turnover of Rs 1000 crore or more, or Net profit of Rs 5 crore or more during any financial year shall constitute a Corporate Social Responsibility Committee(CSRC) of the Board. The committee would comprise of three or more directors, out of which at least one director shall be an independent director. In case the firms are unable to spend the money, they have to provide reasons and disclose the same. The regulation makes it mandatory for the Directors of the company to supervise these spends and to set up a CSR committee to plan, strategize, implement, document and disclose the activities.

Activities which may be included by companies in their Corporate Social Responsibility Policies relating to:—

• Eradicating extreme hunger and poverty;
• Promotion of 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;
• Employment enhancing vocational skills;
• Social business projects;
• Contribution 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.

The rational for CSR activity is that corporate earns their profit by exploiting different resources of the society, therefore, a portion of the benefit derived by them should be spent for the welfare of the society. Though this compulsion may seem burdensome for some companies, it will generate a sense of responsibility among Corporate, particularly when they see benefits in the long term. According to the estimates made by the accounting firm Ernst & Young the implementation of new CSR Law would cover over 2,500 companies in India and generate over U.S. $2 billion of CSR spending in local communities. Even though many of the corporate houses may not get covered by this new provision, it is however important for them also to undertake CSR initiatives to ensure sustainable development of the society and inclusive growth.

Despite the benefits, there has been wide ranging debate on practical applicability of CSR provisions under the companies act. Some of the highly debated loopholes are:

1. CSR as defined under the act has a very wide scope including plethora of issues ranging from environment to poverty, from sustainable development to education etc. The list of activities included in the rules seems to be illustrative rather than exhaustive. At the same time,
an overall reading of the rules strongly suggests that the scheduled activities alone will be considered for the purpose of CSR. Whether or not social activities falling outside the purview of the schedule form a part of CSR activities still remains doubtful.

2. The Clause ‘Comply or Explain’ prescribes that in case of non compliance with the CSR mandate of minimum 2% spending; the target company should come up with a valid explanation for such non compliance. However there is absence of any guidelines in the Act for classifying any explanation as valid or invalid, hence there could be possibilities of arbitrariness.

3. Noteworthy to say that to ensure the compliance of the CSR mandate of the Companies Act there are few clauses incorporated in the Act like presence of independent director in the CSR committee, details about the company’s CSR policy to be furnished in the director’s report, penalty for failure in meeting the requirements of clause 135, but these are not sufficient to rule out the probability of target companies avoiding the CSR mandate. The standing committee on finance has suggested that a monitoring body should be set up to whom the report for CSR activities could be submitted.

4. Making penal provision more stringent: If Section 134(8) is read with Section 135(5) it can be very well made out that the penal provision is only for the non-compliance of submitting the report and not for the failure to spend with respect to CSR.

5. It is reasonable to think that there could be certain companies which have triggering profits and net worth but incur losses have incurred a net loss. The language of the Act suggests that even such a company, after incurring losses, would also be required to mandatorily undertake CSR obligations, as the word ‘or’ has been used i.e. if a company falls in either of the three categories, then clause 135 will apply to it.

6. It believes that the biggest concern for the industry is with respect to the impact of CSR contribution from a tax deductibility point of view. Under the current income tax law, the CSR spending cannot be treated as expenditure. It will be part of profit and attract taxes. Also, the provision of Companies Act prescribes that every target company has to part with 2% of 3 year’s Profit before tax. This will automatically result in double taxation for the companies.

7. Another aspect of ambiguity in the new law that was expected to be corrected through the rules was the 'local area preference'. The Act provides that a company should give preference to the local area in which it operates for CSR spending. However it fails to specify how would this work if a company has more than one operational office, should location of a factory or the corporate office be the target of preference?

**SUGGESTIONS & CONCLUSION**

There is urgent need for more inclusive management of CSR activities where businesses should not view CSR as a hindrance of carrying business in India. Rather CSR presents an opportunity by which India can achieve a balance of social, environmental and economic imperatives and at the same time protecting the interest of various stakeholders. Introduction of CSR provisions is undoubtedly a welcome step to make sure that the target companies come under the legislative purview as far as their spending for social cause is concerned. This is certainly a positive step which can ensure corporate sector’s contribution to equitable and sustainable development especially in case of India where nearly 400 million people still live on less than US $ 2 a day and two third of the population lack access to proper sanitation facilities. CSR spending on environment, energy, education etc will in turn boost capital formation in the long run. This will reduce inefficiencies and accelerate investment. Moreover, such initiatives will also build goodwill, fight business competition and build positive image of the company in the public. Thus it can be a win-win situation for both the public and the businesses.

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