Impact Of The Companies Act 2013 On Corporate Social Responsibility

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ABSTRACT

In an ideal situation, if a company invests in society activities, it would be rewarded by its stakeholders in many ways. It has been the practice of many corporate houses in India to contribute to the society by building educational institutions, hospitals etc. Recognising the need for inclusion of socially unprivileged sections of the society in India's growth story, the new company law of 2013 has come up with a mandate for giant corporates to shell out at least two per cent of their three years annual average profits towards Corporate Social Responsibility (CSR) activities. The law is perhaps the first of its kind in Indian history recognising the scope of utilizing corporate strengths towards fulfilling country's social objectives. Going by the new norms, the two per cent spending on CSR is not mandatory but reporting about it is mandatory. Proper disclosure of the CSR policy by the corporates, reasons for not meeting the required expenditure and various activities that may be included in the CSR agenda of the companies are on the board in the new CSR provisions. Thousands of companies are expected to fall under the CSR obligations which may lead to estimated CSR spending amounting to thousands of crores of rupees. Looking from another perspective, companies pay huge taxes in one form or the other and the money collected from such taxes by the government should take care of the society objectives. Is it really justified to overburden the corporates to spend additional two percent towards social activities? The present research paper attempts to analyse several such aspects of the new CSR law in the context of modern corporate philosophy as also drawing attention of the government authorities towards practical difficulties in the implementation of the new provisions and the possible solutions to overcome these difficulties.

Keywords: CSR Mandate; Companies Act of 2013; Corporate Social Responsibilities, CSR Initiatives.

INTRODUCTION:-

The Companies Act, 2013 ('2013 Act'), enacted on 29 August 2013 on accord of Hon'ble President's assent, has the potential to be a historic milestone, as it aims to improve corporate governance, simplify regulations, enhance the interests of minority investors and for the first time legislates the role of whistle-blowers. The new law will replace the nearly 60-year-old Companies Act, 1956 ('1956 Act').

The 2013 Act provides an opportunity to catch up and make our corporate regulations more contemporary, as also potentially to make our corporate regulatory framework a model to emulate for other economies with similar characteristics.

The 2013 Act is more of a rule-based legislation containing only 470 sections, which means that the substantial part of the legislation will be in the form of rules. There are over 180 sections in the 2013 Act where rules have been prescribed and the draft rules were released by the MCA in three batches. It is widely expected that the 2013 Act and indeed the rules will provide for phased implementation of the provisions and in line with this, 98 sections of the 2013 Act have been notified and consequently the corresponding section of the 1956 Act cease to be in force.

The 2013 Act has introduced several provisions which would change the way Indian corporate do business and one such provision is spending on Corporate Social Responsibility (CSR) activities.

CSR, which has largely been voluntary contribution, by corporate has now been included in law. Basis the CSR provisions, as laid down under the 2013 Act and the draft CSR rules made available for public comments."[1]

The 1956 Act has been in need of a substantial revamp for quite some time now, to make it more contemporary and relevant to corporate, regulators and other stakeholders in India.

While several unsuccessful attempts have been made in the past to revise the existing 1956 Act, there have been quite a few changes in the administrative portion of the 1956 Act. The most recent attempt to revise the 1956 Act was the Companies Bill, 2009 which was introduced in the Lok Sabah, one of the two Houses of Parliament of India, on 3 August 2009.

This Companies Bill, 2009 was referred to the Parliamentary Standing Committee on Finance, which submitted its report on 31 August 2010 and was withdrawn after the introduction of the Companies Bill, 2011. The Companies Bill, 2011 was also considered by the Parliamentary

Standing Committee on Finance which submitted its report on 26 June 2012. Subsequently, the Bill was considered and approved by the Lok Sabah on 18 December 2012 as the Companies Bill, 2012 (the Bill). The Bill was then considered and approved by the Rajya Sabah too on 8 August 2013. It received the President's assent on 29 August 2013 and has now become the Companies Act, 2013.

The changes in the 2013 Act have far-reaching implications that are set to significantly change the manner in which corporate operate in India. In this publication, we have encapsulated the major changes as compared to the 1956 Act and the potential implications of these changes. We have also included, where relevant, the provisions of the draft rules, which have been issued by the Ministry of Corporate Affairs (the MCA) till date for public comments. Such inclusions have been highlighted with an asterix at the end of the sentence (*). "[2]

CORPORATE SOCIAL RESPONSIBILITY: -

The Ministry of Corporate Affairs (MCA) had introduced the Corporate Social Responsibility Voluntary Guidelines in 2009. These guidelines have now been incorporated within the 2013 Act and have obtained legal sanctity. Section 135 of the 2013 Act, seeks to provide that every company having a net worth of 500 crore INR, or more or a turnover of 1000 crore INR or more, or a net profit of five crore INR or more, during any financial year shall constitute the corporate social responsibility committee of the board This committee needs to comprise of three or more directors, out of which, at least one director should be an independent director. The composition of the committee shall be included in the board's report. The committee shall formulate the policy, including activities specified in Schedule VII, which are as follows:

1) Eradicating extreme hunger and poverty.
2) Promotion of education.
3) Promoting gender equality and empowering women.
4) Reducing child mortality and improving maternal health.
5) Combating human immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases.
6) Ensuring environmental sustainability.
7) Employment enhancing vocational skills.
8) 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 and Tribes, other backward classes, minorities and women. Such other matters as may be prescribed."[3]

It is not secret that India is a developing nation-state; it has been the experience that the government machinery has often been unable to reach all those who require its assistance. Further, there are limitations on the activities that the government can indulge in. The private sector is viewed by many circles, sadly, as lacking in its participation in activities that go beyond its balance sheets. With a view to increase private spending on socially responsible projects, the government introduced section 135 to the Companies act 2013 which necessitates all companies above who meet a certain threshold to spend at least 2% of their average profits of the preceding three years on corporate social responsibility projects."[4]

OBJECTIVES:-

Corporate Social Responsibility (CSR), a term widely use for defining the responsibilities of corporate world towards the society & environment. Although the term is not new in this Corporate world but its scope & meaning has undergone major changes from treating it as a mere charity in comparison with the responsibilities/duties of the Corporate towards the outer world.

There are many big entities who have been actively engaged in the CSR activities but unfortunately the number is relatively less. In order to encourage more entities to participate in the process of development of the society via- CSR, the Government of India has actually implemented the concept of CSR in the new Companies Act 2013, On 27th February, 2014, the Government of India has notified the rules for CSR spending u/s 135 of the New Companies Act 2013 along with Companies (Corporate Social Responsibility Policy) Rules, 2014 effective from 1st April 2014."[5]

Recently notified Companies (Corporate Social Responsibility Policy) Rules, 2014 has defined the term "Corporate Social Responsibility (CSR)" as follows: "Corporate Social Responsibility (CSR)" means and includes but is not limited to:

i. Projects or programs relating to activities specified in Schedule VII to the Act; or

ii. Projects or programs relating to activities undertaken by the board of directors of a company (Board) in pursuance of recommendations of the CSR Committee of the Board as per declared CSR Policy of the company subject to the condition that such policy will cover subjects enumerated in Schedule VII of the Act.

Meaning thereby, conducting all those activities which are either specified under Schedule VII to the Companies Act, 2013 or those which are recommended by the CSR Committee of the Board as per the CSR Policy and are undertaken by the Board of directors of the Company will be covered under the scope of activities of Corporate Social Responsibility.

Ministry of Corporate Affairs vide its Notification dated 27th February, 2014 *(which shall come into force with effect from 1st April, 2014)* has come up with the modified Schedule VII which covers wide range of objectives which can be undertaken by the Companies as a part of their CSR initiatives."[6]

The objectives involve the following:

A. Eradicating hunger, poverty and malnutrition, promoting preventive health care and sanitation and making available safe drinking water;

B. Promoting education, including special education and employment enhancing vocation skills especially among children, women, elderly, and the differently abled and livelihood enhancement projects;

C. Promoting gender equality, empowering women, setting up homes and hostels for women and orphans; setting up old age homes, day care centres and such other facilities for senior citizens and measures for reducing inequalities faced by socially and economically backward groups;

D. Ensuring environmental sustainability, ecological balance, protection of flora and fauna, animal welfare, agroforestry, conservation of natural resources and maintaining quality of soil, air and water;

E. Protection of national heritage, art and culture including restoration of buildings and sites of historical importance and works of art, setting up public libraries, promotion and development of traditional arts and handicrafts;

F. Measures for the benefit of armed forces veterans, war widows and their dependents;

G. Training to promote rural sports, nationally recognized sports, Paralympics sports and Olympic sports;

H. Contribution to the Prime Ministers' National Relief Fund or any other fund set up by the Central Government for socio-economic development and relief and welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women;

I. Contributions or funds provided to technology incubators located within academic institution which are approved by the Central Government;

J. Rural development projects.

The above mentioned objectives constitute the CSR activities and the companies which are covered under the provisions of Section 135 shall be required to carry out any one or more of the objectives as specified above along with following its CSR Policy."[7]

SCOPE:-

Initially, CSR emphasized the official behavior of individual firms. Later, it expanded to include supplier behavior and the uses to which products were put and how they were disposed of after they lost value.

METHODOLOGY:-

A large body of literature exhorts business to adopt measures non-financial measures of success. While CSR benefits are hard to quantify, Orlitzky, Schmidt and Rynes."[8]found a correlation between social/environmental performance and financial performance. The business case for CSR"[9] within a company employs one or more of these arguments CSR is the procedure of assessing an organization's impact on society and evaluating their responsibilities. It begins with an assessment of the following aspects of each business:

I. Customers

II. Suppliers

III. Environment

IV. Communities

V. Employees

Triumphant CSR plans take organizations ahead of compliance with legislation and lead them to respect moral values and respect people, communities and the natural environment.

Corporate Social Responsibility is sustainable – involving activities that an organization can uphold without negatively affecting the business goals.

CSR is not only about ecological accountability or having a recycling policy. It is about considering the whole representation of the company, from internal processes to your clients, taking in every step that a business takes during day-to-day operations. Rising economies such as India have also observed a number of companies enthusiastically engaged in CSR activities.

Organizations in India have been quite sensible in taking up CSR initiatives and integrating them in their business processes. It has become progressively projected in the Indian corporate setting because organizations have recognized that besides growing their businesses, it is also important to shape responsible and supportable relationships with the community at large. Companies now have specific departments and teams that develop specific policies, strategies and goals for their CSR programs and set separate budgets to support them. Most of the time, these programs are based on well-defined social beliefs or are carefully aligned with the companies' business domain. "[10]

To investigate the landscape of CSR activities in India, we collected data regarding the CSR policies and practices of top 200 public listed companies in India, which are categorized in "A" category by the Bombay Stock Exchange (BSE) of India.

Given that CSR literature suggests that organizations increasingly use CSR activities to position their corporate brand in the eyes of the consumers and other stakeholders through their annual reports (Sweeney and Coughlan 2008) and websites (Maignan and Ralston 2002), I collected data using these public sources.

I made an exhaustive list of all CSR areas in which the companies work and methodologies employed by them for carrying out the same, as reported by them in these public sources. I coded the areas of work for CSR, by these companies into 7 broad categories, these are 'Education', 'Health', 'Community Welfare', 'Entrepreneurship Development', 'Environment', 'Market Place' and 'Rural Development'.

These areas of societal development work is not related to the core business of the companies examined and is pursued by them on voluntary basis as there is no statutory requirement on any of the corporation to pursue in such activities."[11]

One of the most applauded aspects of the new Company Law regime is the mandatory social spending requirement. 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.

The new Companies Act, 2013, has made it mandatory for companies to be socially responsible by introducing the 'corporate social responsibility' (CSR) regime. Section 135 of the new Companies Act, read with the CSR Rules, mandates companies meeting certain criteria to set aside two per cent of their net profits for undertaking and promoting socially beneficial activities and projects in India"[12]

DESCRIPTION:-

While the intent of the government is noble, it remains to be seen how effective these new regulations will be. There is already significant amount of confusion with respect to the coverage of foreign companies, while the act speaks only of companies registered within India; the rules make specific mention to foreign companies. We expect a clarification on this from the ministry post elections. The rules specify a 5% cap on expenditure on building CSR capabilities, it is unclear as to what these expenses entail. There is also the elephant in the room that is the applicability of tax deductions on expenses incurred for CSR projects. More often than not, CSR expenditure becomes the bone of contention between the tax payer and the tax department. While the courts have sided with the tax payer in cases where the CSR activities have been for the purpose of welfare of local communities and have brought upon useful change in lives of the local populace, or where the employees and their families have benefited from such initiatives. However it is not clear how the department shall view the deductions claimed by the assesses under the mandatory CSR scheme. Further, it is also not apparent as to how the department shall view expenses incurred in excess of the 2% limit by able and willing assesses. This battle, in our opinion shall be fought over a number of years.

The rules envision scenarios where the allocated amount for CSR may not be fully utilized, however it is not clear whether mere disclosure of the same by the board would absolve the company from the responsibility to spend the unutilized portions or if such monies would accrue to the planned spends from subsequent financial years. There is also the issue of corporate governance, small companies of two directors will see a curious situation where the two directors are not just framing the policy but also implementing it and in their capacity as share holders reviewing the results."[13]

CONCLUSION:-

Considering the increasingly vast and complex business environment, the move of the Ministry of Corporate Affairs is a welcoming step which apart from contributing towards society, plays a major role in various ways which includes attracting and retaining employees in a such a way as to increase morale of the employees along with creating a sense of belonging to the company and contributes towards enhancement of company's own goodwill, positive image along with bringing competitive advantages. Also, as rightly mentioned by United Nations Industrial Development Organization (UNIDO), 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 at the same time addressing the expectations of shareholders and stakeholders.

Ascent Representative,

Ascent International Journal for Research

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