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In India, a legislative reform is needed to push corporate social responsibility

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The corporate social responsibility (CSR) movement began as a response to advocacy for corporations to play a role in ameliorating social problems due to their economic power and overarching presence in daily life.

Now, the movement is transitioning from its reliance on purely voluntary activity to the greater use of laws. The push for legalisation came because voluntary CSR presented problems such as free-riding (companies taking advantage of benefits without actually spending), greenwashing posing as CSR, and false disclosures.

Governments are now modifying their laissez-faire approach and considering legal rules.

The US Securities and Exchange Commission, for instance, has moved beyond its mandate as a market regulator to issue rules on conflict minerals, resource extraction payments, and gender diversity. And, in 2014, the European Union issued a directive on disclosure of non-financial and diversity information.

Similarly, Australian companies are required to disclose how they will manage their environmental
India at the forefront

India has gone further than any other country. In 2013, it enacted Section 135 of the Indian Companies Act prescribing a mandatory “CSR spend of 2% of average net profits ... during the three immediately preceding financial years” for all companies meeting specified financial thresholds. In other words, companies “having net worth of rupees five billion or more, or turnover of rupees ten billion or more or a net profit of rupees fifty million or more during any financial year” have to ensure that they spend 2% of average net profits made during the three preceding years on CSR activities.

In order to assess the effectiveness of this unique experiment in mandating CSR spending and disclosure, we studied the reporting practices of the four largest banks by market capitalisation in India compared with banks from Australia, China, and Japan where there is no such law. In order to do so, we assessed annual and CSR reports of our sample of companies from 2012, one year before the law was passed.

Indian banks did not have CSR reports before 2012. The CSR committees formed by the banks function in the spirit of the law within defined targets, monitoring CSR spend, and reporting reasons for shortfalls in spending.

Of the Indian banks evaluated, only the State Bank of India (SBI) disclosed its CSR spend prior to the promulgation of the new Companies Act; all banks disclosed this spend from 2013.
Despite the new law mandating a CSR spend of 2% of pre-tax profit for corporations of this size, only ICICI Bank met the target in 2014. But it fell to 1.9% in 2016. Kotak Mahindra Bank reported a CSR spend of less than 0.69% of pre-tax profits in 2016.

In spite of not meeting the targeted CSR spend, none of the banks reported any fines or proceedings for breaching the law.

During this period (2012-2016), Australian banks had the highest disclosures, followed by Japan, China and India.

There’s a marginal difference in Indian bank disclosures after the new law was passed in 2013. But these differences may well be due to the different cultures and other non-market factors at play.

**Different programs**

Indian banks spend on educational and health promotional CSR activities, as prescribed by the new law. Additionally, all Indian banks use in-house foundations and centres, and promote staff volunteering at high-profile events. All these activities are designed to obtain maximum positive media coverage.

Less popular CSR activities, such as programs for eradicating malaria or combating other major communicable diseases – also defined in the Act as designated CSR activity – do not get any attention.

Another popular CSR activity is contributing to natural disaster relief funds, which is probably aimed at scoring brownie points with the political party in power. Then there’s lip service to environmental sustainability by the development of “ideal” bank branches with small environmental footprints. But the vast majority of offices languish with old energy-hungry, environmentally dated structures and activities.
In contrast – and despite the absence of a legislative mandate – Australian banks have been disclosing their CSR expenditure since at least 2010. CBA and Westpac spend more on CSR as a percentage of pre-tax profits than the other two major Australian banks.

Chinese and Japanese banks report on targets and achievements to meet their respective environmental laws, albeit not in as much detail as Australian banks. As there’s no legal requirement to report on their actual CSR spends, Japanese banks did not disclose this in their reporting media till 2015.

In 2016, Japanese banks Nomura and Mizuho started reporting their CSR spend. Similarly, Chinese banks started voluntarily reporting their CSR spend in 2016.

But all fall below 0.25% of post-tax profits.

**Time for reform**

Our analysis shows that the law in its current form is failing to promote CSR activity. Its poor design and lack of clear obligations, set in a milieu of poor law enforcement, is also not generating an ethical obligation to obey the law in spirit.

Our findings are of value to policy makers and suggest it’s time to reform laws – to socialise corporations and CEOs in terms of their legal obligations and the benefits of CSR activity, to design enforcement mechanisms, and to generate ethical behaviour.

India’s legal provisions contain vague language and permit a high degree of self-interpretation that undermines legislative intent. For example, it allows banks to list “staff training in fire safety” as part of CSR even though this should be a strictly mandatory workplace safety activity.

Indian banks’ annual and CSR reports do not show a major shift in the nature of disclosures after 2013. The law is perhaps purely expressive as the provision stipulates minimal penalties for non-compliance and relies on a comply-or-explain philosophy. This exacerbates the lack of ethical
obligation to obey laws in India where there's a level of high corruption, low levels of public confidence, weak institutions, low levels of development, and education, among other such issues.

The provisions also appear to be formulated based on a traditional understanding that top management is solely responsible for ethical behaviour and CSR activity, without making the connection between the company and its stakeholders. There is no explanation for how the CSR provision fits within the wider ambit of a corporation's role and purpose, the duties expected of its directors, or the information it is expected to disclose.

Until such time that the law is made more precise and backed up by effective enforcement and penalties for non-compliance, it will not promote CSR or make companies engage more with stakeholders. Section 135 is merely a stealth tax and will impose unnecessary compliance burdens.