ISSUES AND CHALLENGES IN MANDATORY CSR

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ABSTRACT

The emergence of the term Corporate Social Responsibility brushed away the conventional views of a business entity to operate in isolation from society. It not only challenged the rigid concepts of business competition, profitability, and survival but also gave rise to a sense of responsibility to operate in society. A company devoted to CSR is also gaining a reputation in the eyes of shareholders, investors and the general public alike. This study focuses on the issue and challenged faced by the Indian companies in complying with CSR. The study has been conducted using an exploratory research method. The data has been collected from secondary sources but the special focus has been given to a report conducted at the University of Waikato. The research revealed that there are several drivers or motivators to CSR, specifically, to build a positive image of the company or ethical-moral reasons. Similarly, there are several barriers to CSR discussed in the study which include Lack of technological know-how, no impact on employee productivity, etc. the study concluded by listing out the issues and challenges faced by companies due to mandatory CSR. The challenges include ambiguity in income tax rules, fear of overinvestment in a single sector, etc. some small companies still do not understand the significance of being socially responsible and claim that the mandatory CSR is just a duty they are entrapped with because it doesn’t benefit them in any way. On the other hand, large companies which are really conscious about their image tend to invest in CSR activities because they feel more connected to the society after doing so. So, it is essential that awareness about the need for CSR activities is spread and all companies, big or small, are made a part of it so that they pursue these activities with compassion and empathy than due to mere obligation.
The study concludes by suggesting that like the Government amended the legislation relating to CSR in 2019 to specify the direction of the spending along with how to deal with the unspent amount, it can also further amend it to reassure improved spending on CSR activities.

**KEYWORDS – CSR, corporate social responsibility, Section 135**

1. INTRODUCTION

“Social responsibility (is the) responsibility of an organisation for the impacts of its decisions and activities on society and the environment through transparent and ethical behaviour that is consistent with sustainable development and the welfare of society; takes into account the expectations of stakeholders; is in compliance with applicable law and consistent with international norms of behaviour; and is integrated throughout the organisation.”

The Ministry of Corporate Affairs made CSR mandatory in India from 1st April 2014 under Section 135 and Schedule VII of the Companies Act, 2013. The rules were initially applicable on companies with a net profit of at least Rs 5 crore or with a turnover of Rs 100 crore or having a net worth of Rs 500 crore. The companies had to spend 2 percent of their three-year average annual net profit on CSR activities in each financial year, commencing from the financial year 2015. The said Act was amended and further replaced by the Companies (Amendment) Act, 2019, which came into effect on July 31, 2019. The emphasis of the amended Act was on CSR outlay.

The Companies (Amendment) Act, 2019 directs the eligible companies to transfer their unspent CSR funds to one of the funds given under Schedule VII of the Act (e.g. The Prime Minister Relief Fund) within six months of the end of the financial year and also divulge the reasons for such non-spending in their annual statement at the end of the year.

1.1 Treatment of unspent amount

According to the CSR guidelines issued by the Ministry of Corporate Affairs under the Companies Amendment Act 2019,

“If the unspent amount of CSR relates to an ongoing activity, (which is mentioned in the schedule vii) it should be transferred to a special account to be opened by the company in that behalf for that financial year in any scheduled bank to be called the Unspent Corporate Social Responsibility Account, within 30 days

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of the close of the financial year. and such amount shall be spent by the company within a period of three financial years from the date of such transfer, failing which, the company shall transfer the same to a Fund specified in Schedule VII, within a period of thirty days from the date of completion of the third financial year. If the unspent amount is not relating to ongoing activity, it should be transferred by the company to the funds specified in schedule VII, within 6 months of the expiry of the Financial year.

If CSR provisions are violated, the company is accountable for a minimum fine of INR 50,000 which may be extended to INR 25 lakh. Also, the defaulting officer of the company may be liable to imprisonment for up to three years, or a fine up to INR 5 lakh, or both.”

2. RESEARCH OBJECTIVES

- To explore the challenges and issues faced by Indian companies in implementing CSR.
- To study the drivers in implementing CSR.
- To study the barriers to CSR.
- To give recommendations for fast-tracking CSR inventiveness in India.

3. LITERATURE REVIEW

In the study, “Analysis of mandatory CSR expenditure in India: a survey”3, the author has revealed that the most significant encouraging factors for Indian corporations undertaking CSR activities are to enhance their image in the public eye. He also mentioned the drivers and barriers to CSR which have been mentioned in the study.

Various drivers have been studied for CSR expenditures in literature where Researchers have proposed numerous drivers for CSR uses with two perceptions: good and vital (Dhanesh, 2014). The ethical point of view of stewardship hypothesis recommends that organizations participate in socially mindful practices since it is 'the right thing to do' and that organizations are or should be propelled by fundamental traits, for example, moral qualities and good authority (Bansal, 2003; Donaldson and Davis, 1991; Heugens and Kaptein, 2008; L'Etang, 1994).

Conversely, the vital point of view of the asset-based hypothesis recommends that organizations participate in CSR due to inspirations in light of the fact that it proves advantageous, for example, expanded worker responsibility and client dedication, and a maintainable upper hand.

McWilliams and Siegel (2011), considered CSR as a 'co-specific resource' that can be used to upgrade the estimation of the company's general disrepute for quality or a specific brand of its item. An audit of the

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2 http://www.mca.gov.in/SearchableActs/Section135.htm
present writing identifying with Indian corporates uncovers a diverse assortment of discoveries on these two drivers. A dominating arrangement of studies buys into the key point of view of CSR, contending that organizations in India participate in CSR for its reputational, monetary, and social advantages (Mehra, 2006; Mitra, 2007; Sagar and Singla, 2004; Sharma, 2011; Sood and Arora, 2006).

Singh and Narwal (2012) demonstrated that the Indian firms are exceptionally calculative, i.e., they will release CSR in the zone where there is a more prominent possibility of developing a positive picture and a brand or corporate image, and they are agreeable to self-guideline and by and large, restrict outer guidelines in the event that they are forced by governments. Be that as it may, a few examinations have discovered that CSR in India is driven essentially by top executives' sense of ethics. (Arevalo and Aravind, 2011; Gopinath, 2005; Lee, 2010).

4. RESEARCH METHODOLOGY

This study is an effort of exploratory research, grounded on various sources of secondary data available from journals, magazines, articles and media reports. A descriptive study has been undertaken keeping in view the requirements of the study. Blog articles, newspaper clippings, old survey reports, previously researched journals, Books and Websites were used which were enumerated and recorded. Also, authentic data from the study conducted by Abhishek Mukherjee has been analyzed in the study. The above-mentioned author had conducted a detailed survey from 223 respondents, who were divided between two types. One is the one who had an obligation to spend resources on CSR activities and those who were not. The respondents comprised of companies of diverse size, businesses, and areas. The surveys conducted by the abovementioned author were finished by the top-level management within each company, i.e., Director, MD, CEO, CFO or Senior Manager.

5. FINDINGS OF THE STUDY

“What corporations do to society is far more important than what corporations can do for society”

-Peter Drucker

The concept of CSR saw a major transformation from being a mere philanthropic measure of a corporate entity to becoming an indispensable part of it. Yet there seems to be a lot of issues that may make corporate houses feel that these legal obligations have entrapped them into becoming responsible by


5 hbr.org/2010/06/how-did-peter-drucker-see-corp
force. Yet, with the fear of climate change wrapping the world under its arms, the general public is
becoming more aware of the social issues and expect the companies to address these issues.
The “2017 Cone Communications CSR Study” revealed that seventy-eight percent of people want
corporations to address significant social justice issues. \(^6\)

According to the report ‘Responsible Business Rankings 2018’ by IIM Udaipur and Futurescape Tata
group companies occupy the key position in CSR activities in India.

5.1 Issues and Challenges of Mandatory CSR

- **Duplicity or overinvestment**

It is possible that companies working in the same region may end up spending more than required in a
particular area or sector. Good CSR initiatives by a company can also be copied by another company
which can lead to regional inequalities.

- **Ambiguities in provisions of income tax**

CSR spending is not considered to be an expenditure. Currently, the provisions relating to CSR in the
Income Tax Act have some ambiguities that need to be solved. While corporates might get comforted
from their CSR Expenditure compliance obligations but the real spirit of CSR actually remains
unsatiated. To guarantee that the corporate Social responsibilities are complied with in its full vigor and
essence by a corporate entity, it is essential to redefine the CSR provisions in the Income Tax Act.

- **Uneven cost on small corporate entities**

For new or growing companies, mandatory CSR has posed a threat as these companies solely rely on their
net profit as a source of capital (retained earnings).

- **Ambiguous CSR guidelines regarding initiatives**

Some corporate entities find it frustrating that there is no fixed amount to be invested in CSR projects, it
depends on the size and profitability of the company. i.e. bigger and larger the company, bigger is its
share of CSR initiatives.

\(^6\) [https://www.conecomm.com/research-blog/2017-csr-study](https://www.conecomm.com/research-blog/2017-csr-study)
• **Lack of empathy in companies**

Since CSR is mandatory in India, it is possible that the entire purpose of making companies socially responsible will lose its significance. Each company will try to allocate the necessary resources to fulfill their mandatory duty rather than empathizing and trying to solve the real problems in the required areas.

• **Lack of participation by communities**

There is an information gap between the company and the community that needs to be resolved.

• **Lack of transparency**

Lack of transparency by companies and agencies working towards implementing CSR often leads to a lopsided trust between corporate entities and local communities.

### 5.2 DRIVERS OF CSR SPENDING IN INDIA

The research studied the 15 drivers and 13 barriers for CSR spending in India. The drivers for CSR expenditure are given below –

- Improve the image of the business
- Company’s apprehension for its business/social accountability
- Intensify marketing and public relations
- Improve relations with public administration (public/state authorities)
- Improve the economic performance of the company (costs’ reduction, sales’ increase)
- Improve customers’ trustworthiness
- Ethical/moral reasons
- Company’s concern for the environment
- Apply/implement business code of conduct
- Establish and/or retain competitive advantage
- Improve relations with business partners and investors
- Improve employees’ job satisfaction
- Company’s philosophy and traditions
- Increase productivity per employee
- Help in the recruitment and retention of suitable employees

### 5.3 BARRIERS TO CSR SPENDING IN INDIA

- Inadequate free cash flow to undertake CSR activities.
- Inadequate state/government support to cause it to undertake CSR activities.
Lack of technological know-how.
Lack of human resources to undertake CSR activities.
CSR expenditure was perceived not to have a favourable impact on financial performance.
Inadequate public support/pressure to cause it to undertake CSR activities.
Increase operating costs.
No impact on employee productivity.
Competitive disadvantage if the money spent funds on CSR activities.
No favourable impact on the market value of the company.
CSR expenditure perceived not to have a favorable impact on the market risk of the company.
Change in management leads to a withdrawal of support for CSR activities.
No impact on customer loyalty

5.4 CSR – BOON OR BANE?

Ever since the passing of the mandatory regulations for CSR in India, there has been long debate whether it will be fruitful for society or not. Business houses have time and again spoken against the mandatory law of practicing CSR. In a developing country like India, where we are still fighting with issues like poverty, hunger and sanitation, where people still live below poverty line, this effort of the Ministry of Corporate Affairs should be seen as a positive move forward to ensure that corporate houses making profits contribute their share to the betterment of the society as a whole. The companies which are perceiving this law as an obligation that they have to fulfil every year, should change their mind set and view this law as an opportunity to work for the society. They should know that CSR has its own benefits. It will not only help to increase the standard of living of people in the society where the business operates, but it will also help in developing a good will among their investors, consumer, and government at large.

Yet there are many arguments against the mandatory CSR. In the words of Rohini Nilkeni, the wife of Nandan Nilkeni, a philanthropist, “Every life form has its role and purpose. It is dysfunctional for steel or aluminum companies to run schools or hospitals. Ticking a CSR checklist or writing a cheque out of profits is a poor substitute for being a good corporate citizen because how companies make profits (ethically and legally) is more important than what they do with them (dividends or taxes). But mandatory CSR over and above taxation, forces companies to do the government’s job. And trying to outsource the state’s primary job is a bad idea. Companies should create jobs and pay taxes. It is unrealistic and unfair to expect them to focus beyond the immediacy of circumstances (survival and growth) that is the life of most small entrepreneurs.”
6. **SUMMARY**

This study gave an in-depth understanding of the drivers or motivating factors that are reasons for corporations to take on CSR spending. Based on the survey of 223 companies conducted in the study Analysis of mandatory CSR expenditure in India: a survey the most significant drivers of CSR spending are concerns for the company’s brand image, and the wish to improve the corporation’s relationship with the external business environment. The study also revealed that top-level management is mostly motivated by the aim of distinguishing the business house for tactical details rather than due to ethics and morality. Large companies spend lavishly on CSR because they are concerned for the society and environment and new companies are solely driven by the motivation to make their image better and attract clients who are slowly drifting towards an environment-conscious investing. It can’t be denied that not many large-cap companies spent lavishly prior to the mandatory regulation related to CSR. But that wasn’t because they weren’t concerned about the society, but because they had cash constraints to deal with or they had no idea which sectors to invest in. Today, many small companies still don’t encourage CSR activities because they believe it is not a part of their strategic plan, neither it will benefit them in any way.

7. **CONCLUSION**

To address the issues mentioned above, an agency can be set up at the central and state level to coordinate the efforts of the CSR implementing companies and manage the spending of companies. It will help in solving the problem of irregular investment in different sectors in different regions. Also, in order to implement the best possible CSR practices resources can be pooled. There is a limited number of activities permitted under schedule 7 of section 135 but the list can be broadened and sensitive issues like Human Rights, and Disability can also be included. Corporates are also concerned about the unspent amount being transferred to the Prime Minister’s National Relief Fund. This is because the said fund isn’t a government body, hence there is an absence of accountability. Steps can be taken to remove the fund from the list so that the doubts of the companies are addressed. There are many companies that consistently work for the well-being of its employees – from top-level to lower level. Those acts are not included in CSR activities. It can also be done. Last but not the least, the ambiguity relating to the income tax act and CSR outlay not being considered expenditure can be solved by a necessary amendment in the Income Tax Act, 1961 and CSR spending should be made deductible, as it can’t be denied that this spending is an essential part and parcel of business.

The victory of CSR lies in the company’s commitment to it by treating it as a responsibility than an obligation. It is significant for the business segment to classify, and encourage effective strategies that accomplish threefold wins- returns, environment sustainability and maintain social justice.

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8 Verdict by CIC, A.K Goel vs PMO, 2009
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