Unveiling Blind Spots: Corporate Social Responsibility

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Corporate Social Responsibility (CSR) involves companies choosing to actively contribute to societal improvement and environmental preservation. As per the **World Business Council for Sustainable Development,** “Corporate social responsibility is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large”.
Nevertheless, **Section 135 of the Companies Act, 2013** [1] mandates certain companies to allocate at least 2% of the average net profits from the preceding three financial years to CSR endeavours in every financial year. An affidavit issued by the Ministry of Corporate Affairs in **Mohd. Ahmed v. Union of India** [2] defined CSR as an activity covered under Schedule VII of The Companies Act, 2013 which is carried out by a Company, which forms a part of its core business, if not done with a profit motive.
CSR obligations in India are applicable to companies meeting any of the following criteria in the preceding financial year:
a. Net worth exceeding Rs. 500 crore
b. Turnover surpassing Rs. 1000 crore
c. Net profit exceeding Rs. 5 crore
Though the CSR has been made mandatory in India, it is an evolving concept with its set of challenges and complexities. From lack of clear guidelines and issues of transparency,

various obstacles hinder the effective implementation of CSR initiatives. In this comprehensive analysis, we delve into the multifaceted challenges faced by corporations and stakeholders involved in CSR activities in India.

1. Regional Disparities:

Regional and sectoral disparities in CSR spending highlight the unequal distribution of resources and attention. The first proviso to Section 135 (5) states that the company shall give preference to the local area and areas around it where it operates, for spending the amount earmarked for CSR activities. According to the most recent report of MCA, Maharashtra, Gujarat and Karnataka, received the largest share of CSR funds, with Maharashtra alone receiving 13.21 per cent of the total during FY 2020-21.3 In contrast, the northeastern states of Assam, Arunachal Pradesh, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, and Tripura received a mere 0.91 per cent of the funds in FY 2020-21. [3]

To address this, the High-Level Committee (HLC) [4] appointed by the MCA in 2018 had recommended that a clarification be issued advising companies to engage in CSR activities by balancing local area preference with national priorities.

2. Sectoral Disparities:

Regional disparities are coupled with a disproportionate focus on certain sectors like education and healthcare, neglecting the needs of marginalized communities, rural development and environmental conservation efforts. According to filings made by companies in 2021, education sector and health sector received 37% and 30% of total CSR expenditure respectively. On the other hand, only 9% of CSR expenditure was contributed towards rural area development.

3. Identification of Suitable Implementing Agencies (IAs):

The success of CSR initiatives frequently hinges on collaborations with non-governmental organizations (NGOs). Yet, the inadequate recognition and lack of structure among numerous NGOs in India present difficulties for corporations in search of dependable partners. Moreover, the absence of well-established NGOs in remote and rural areas adds complexity to the task of identifying and fulfilling community needs, resulting in limited contributions to rural development. For companies involved in CSR activities, the persistent challenge lies in identifying suitable implementing agencies. The National CSR Exchange Portal has been introduced to tackle this hurdle by facilitating connections between companies and social welfare projects. Nonetheless, challenges such as technological compatibility and data accuracy persist.

4. Misuse by Trusts:

Instances of misuse commonly occur when companies rely on trusts to execute their CSR projects. For instance, if a company is mandated to allocate, let’s say, Rs 20 crore towards CSR, it issues a cheque to a trust. Subsequently, the trust deducts its commission and surreptitiously returns the remaining amount in cash to officials or promoters, effectively converting Rs 20 crore of legitimate funds into illicit funds. While certain states like Maharashtra have enacted laws such as the Bombay Public Trusts Act, 1950, trusts across the country lack uniform regulation. Hence public trusts are often exploited for money laundering due to insufficient governance and oversight.

5. Indirect Contributions to Political Parties:

The issue of indirect contributions to political parties adds another layer of complexity to CSR activities. Recommendations HLC emphasize the importance of due diligence in evaluating the nexus between implementing agencies and political entities, highlighting the need for transparency and accountability in CSR partnerships.

6. Companies who are Exempted from Filing Financial Statement:

Companies exempted from presenting financial statements as outlined in Schedule III of the Act include insurance or banking companies, as well as those involved in electricity generation or other specified classes of companies. Instead, these companies adhere to a specific form of financial statement stipulated in or under the Act governing their respective class. Despite their engagement in CSR activities, these companies often fail to disclose their expenditure, resulting in a lack of transparency. The number of companies reporting on CSR, exempted from Schedule III requirements, has steadily decreased from 1000 in 2014-15 to 716 in 2017-18, according to data provided by HLC.[5]

7. Lack of Transparency and Information:

Transparency is a cornerstone of effective CSR governance, yet many corporates fall short in disclosing relevant information about their CSR activities. The absence of time-bound audits contributes to a lack of transparency in CSR activities. Many Indian companies refrain from disclosing information about their CSR initiatives and expenditure, undermining efforts to build trust and accountability with stakeholders. This lack of transparency hampers trust-building efforts and hinders stakeholders' understanding of the impact of CSR initiatives.

8. Greenwashing:

The occurrence of greenwashing, where companies superficially engage in CSR activities solely for compliance purposes rather than genuinely contributing to social or environmental betterment, compromises the credibility of CSR endeavors. In the absence of compelling enforcement mechanisms, greenwashing practices endure, perpetuating skepticism and diminishing trust in corporate social responsibility.

9. Lack of Focus on Sustainability:

Many CSR-funded initiatives prioritize short-term goals over long-term sustainability. It is imperative to develop initiatives that only address immediate needs and do not contribute to lasting social and environmental impact.

10. Lack of Specific Penal Clauses for Non-Compliance:

The amendment in 2020 provides a specific penal clause in sub-section (7) of section 135 which only provides with respect to "Failure to transfer unspent amount to the fund specified in Schedule VII or in the case of ongoing projects to the special account as required by sub-section (5) or (6) of section 135". There is absence of specific penal clauses for issues like non-constitution of CSR Committee, insufficient CSR Policy, failure to disclose CSR Policy contents, and non-filing of CSR Annual report with insufficient particulars leaves room for non-compliance without strict consequences. Such non compliances can only be addressed under the general penal clause of section 450 of the Companies Act, 2013. However, this might not provide sufficient deterrence for CSR non-compliance.

11. Applicability to Various Business Entities:

The scope of CSR application be expanded to include Limited Liability Partnerships (LLPs) that fall within the jurisdiction of the MCA. CSR may also be extended to banks licensed under the Banking Regulation Act of 1949. The applicability of CSR rules may also be extended to similarly situated entities not covered by the Companies Act by making relevant revisions to the Companies Act and, if necessary, their individual statutes.

12. Lack of Expertise and Strategic Planning:

The lack of technical expertise or subject knowledge among CSR committees and strategic planning hampers effective planning and implementation of CSR projects. Engaging qualified CSR professionals and prescribing eligibility criteria can enhance the effectiveness of CSR governance structures. Without strategic planning, companies struggle to identify and invest in high-impact CSR projects.

Way Forward:

1. Sectoral Balance: It is imperative for companies to prioritise environment restoration, rural area development, gender equality, sports, etc. This will lead India to achieve sustainable development goals.
2. Community Participation: All CSR projects should involve active participation from communities, district administration, and public representatives in the selection and implementation processes.
3. Enhanced Monitoring: The CSR framework should incorporate recommendations from the high-level committee of 2018 to strengthen the monitoring and evaluation system. This includes making CSR part of statutory financial audits by including CSR spending details in a company's financial statements and mandating independent third-party impact assessment audits to prevent duplication and fraud. Additionally, the MCA and line departments should increase direct monitoring and supervision over companies' spending.
4. Coordination with NGOs: Companies and Non-Governmental Organisations should collaborate to pool resources and build synergies for more efficient and effective implementation of CSR activities.

In conclusion, addressing the myriad challenges related to CSR activities in India requires a holistic approach involving collaboration between government, corporations, NGOs, and communities. By fostering transparency, accountability, and strategic alignment with sustainable development goals, India can leverage CSR as a powerful tool for social progress and environmental stewardship.

References-

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