India’s mandatory CSR policy: implications and implementation challenges

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Abstract: The increasing emphasis on social responsibility across the world is not new (Warhurst, 2005) and many countries require companies to disclose information about their environmental, social and employee-related impact, as well as their diversity policy (The Hauser Institute, 2015). India took CSR to the next level by mandating it for all companies through the recently introduced Section 135 in the Companies Act (2013). The provisions of the section require companies to establish a CSR committee consisting of three members of the Board of Directors to develop a CSR policy and review the CSR activities and prepare periodic reports. The above mentioned CSR infrastructure therefore necessitates significant capacity building within companies. With respect to implementation, companies may channel their resources through qualified non-governmental organisations (NGOs). Consequently NGOs will also require significant capacity building. In this paper we identify the implications of the new guidelines that are worthy of consideration; these implications are for companies that meet the criteria to and therefore must comply with the provisions contained in Section 135, the organisations (including NGOs) that will implement the activities and other general implications. Furthermore the paper suggests mechanisms by which several of these challenges can be met and managed.

Keywords: mandatory CSR; companies; non-governmental organisations; NGOs; compliance; capacity building; CSR implementation; CSR board; CSR policy Section 135; Schedule VII.

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1 Introduction

The increasing emphasis on social responsibility across the world is not new (Warhurst, 2005) and many countries require companies to disclose information about their environmental, social and employee-related impact, as well as their diversity policy (The Hauser Institute, 2015). Indonesia was the first country in 2007 to mandate corporate social responsibility (CSR) but it was “limited to companies which have an impact on natural resources” [Waagstein, (2011), p.460]. India took CSR to the next level by mandating it for all companies through the recently introduced Section 135 in the Companies Act (2013). Mandating CSR may sound like an oxymoron (Kowalski, 2016), but mandating CSR is what the recent introduction of Section 135 has indeed done. The new section prescribes, for companies, an expenditure on CSR activities in their respective geographical areas of operation in an outcome and time-driven manner.

This paper is motivated by a number of factors. First and foremost, mandatory CSR is a new phenomenon around the globe and there is no previous knowledge of the implications of such a CSR regime. Although many companies around the world engage in activities that fit under the CSR label, there are mixed opinions about the alignment between the fundamental goal of a business and the goals of CSR activities (Cooke, 2010; Friedman, 1970; Hillman and Keim, 2001; Sankar, 2015; Warhurst, 2005). In this regard, Kowalski (2016, p.86) observes as follows: “despite our best endeavours to find a business case for CSR the oxymoronic tension between the interests of the firm and society will not go away”. In contrast, Brammer and Pavelin (2005) and Godfrey et al. (2009) are more positive and provide evidence to conclude that investments in CSR provide an insurance like effect which, in turn, can help companies at least preserve their financial performance when faced with a negative event. Similarly, Vogel (2005, p.45) also offers support for the argument that there is a business case for virtue. In this context of mixed opinions regarding voluntary CSR, the idea of mandatory CSR is an interesting phenomenon.
It is widely held that CSR is a voluntary activity (Dahlsrud, 2008); however, Venkatesan (2013) observes that several recent initiatives across the globe suggest a move in favour of more non-voluntary frameworks of accountability towards a broader set of stakeholders. Moreover, the United Nations Industrial Development Organisation (UNIDO) views CSR as a way in which companies can help governments achieve a balance of economic, environmental and social imperatives.

A paper recently published by the Hauser Institute (2015) suggests that India is the only country with a mandatory CSR policy for all companies. The only other country that mandates CSR is Indonesia but this is “… specifically limited to companies which have an impact on natural resources” [Waagstein, (2011), p.460]. Most other countries only have disclosure/reporting requirements.

Secondly, as many as 16,000 companies may meet the criteria and therefore be required to invest in CSR, as suggested by participants attending a summit on CSR in May 2015; many of these 16,000 companies are not likely to have previous experience with CSR. Therefore it is important that they clearly understand the implications of Section 135 and the challenges associated with its compliance.

Thirdly, anecdotal evidence suggests that the level of preparedness, especially among smaller companies and many partnering non-governmental organisations (NGOs), is limited at best, which can seriously delay the implementation of CSR projects. The recently introduced Section 135 allows companies to implement their CSR projects either through their own foundations or in partnership with NGOs. Therefore, company-NGO partnerships are essential for effectively implementing CSR activities, as well as ensuring the sustainability of such projects (Ernst & Young, 2013). Similarly NGO capacity is also essential for the successful implementation of CSR projects initiated under this section.

Finally, we are not aware of any prior research that outlines the implications and implementation challenges of Section 135 in a comprehensive manner. The purpose of this paper is to address this gap in the literature and, in the process of doing so, identify and elaborate upon the implications and implementation challenges and offer some suggestions to address them.

The rest of this paper is structured as follows. The next section briefly introduces Section 135, following which the broad implications of the provisions of the section are discussed. Following this, the implementation challenges from the perspectives of companies and NGOs are outlined and discussed in the next two sections. The final section concludes the paper by providing a summary, limitations of the paper and future research.

2 Section 135

The focus on a broader group of stakeholders, rather than just shareholders, is not new to India. Many large business houses have traditionally paid attention to the needs of employees and the society at large. For example, Jamsetji Tata, founder of the Tata Group, believed that wealth generated through business must be shared with society (Mukherjee, 2008; Sivakumar, 2008). Cappelli et al. (2010) also note that the focus on a broader mission is a uniquely ‘Indian way’ of conducting business. India has achieved significant outcomes in socio-economic development; however, a significant portion of the Indian population still struggles. Besides, although government initiatives usually start off with lofty ideas, many have failed miserably due to poor implementation. These
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factors, especially the latter two, offer a compelling reason for greater involvement of businesses in the country’s social development agenda, both from a resource perspective as well as to utilise the expertise of businesses in planning and implementation. According to Dr Bhaskar Chatterjee, CEO and Director General of the Indian Institute of Corporate Affairs, “Section 135 … evolved over a period of time through much debate, discussion and consultation between … corporates, government, parliamentarians, civil society, NGOs, etc. It embodies the essence of the development sector … [that] India really needs today – active involvement of corporate India in nation building” (Forbes India, 2013).

The introduction of Section 135 represents a major milestone in attempting to change the way business and society engage with each other. The recent revision mandating qualified companies to contribute a minimum of 2% of their average net profit earned during the three immediately preceding financial years towards CSR opens the door to significant investments in social, environmental and economic developmental activities across the country. According to Clause #1 in the section every company with a net worth of at least ₹500 crores (USD 75.3 million), a minimum turnover of ₹1,000 crores, or a minimum net profit of ₹5 crores during a given financial year “shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director” [Government of India, (2013), p.80]. According to Clause #3, the CSR committee’s roles are to formulate and recommend a CSR policy to the Board, recommend the expenditure level that the company should incur and monitor the CSR policy on a periodic basis. According to clauses #4 and #5 the company’s Board must approve and disclose the CSR policy and ensure that the minimum prescribed CSR amount is spent on activities recommended by the CSR committee (Government of India, 2013). The company’s net profit calculation excludes any profit from its overseas branches or companies, as well as any dividends received from other companies in India. However, foreign companies doing business in India, whether by themselves or through an agent or even electronically, are included under the new provisions.

The Act allows companies to implement planned CSR projects through their trust or foundation, or by partnering with established NGOs; companies may also pool their resources and invest in CSR. The prescribed CSR activities are listed in Schedule VII of Section 135 and include areas such as promotion of education, gender equity and women’s empowerment; combating HIV/AIDS, malaria and other diseases; eradication of extreme poverty; contribution to the Prime Minister’s National Relief Fund and other central funds; social business projects; reduction in child mortality; improving maternal health, environmental sustainability and employment enhancing vocational skills. Upon closer scrutiny one cannot miss the point that the focus of schedule VII is largely on the social dimension and to a lesser extent on the economic and environmental dimensions. Recent studies suggest that healthcare, education and community development are preferred areas of CSR activity among Indian companies (Chandra and Kaur, 2015; Rai and Bansal, 2014).

Schedule VII offers considerable autonomy to companies in designing their CSR agenda, and it will no doubt be interesting to watch how companies choose projects from among the wide range of options. More specifically it will be interesting to observe the extent to which companies will invest their CSR funds merely to comply with the Act versus investing with the intent of meaningfully contributing to social development. A reason why companies themselves will benefit from undertaking CSR activities is the fact
that several of them have by now realised that the ‘licence to operate’ is no longer given by governments alone, but by communities that are impacted by their businesses (Warhurst, 2005). A CSR program that meets the aspirations of these communities not only provides them with the licence to operate, but also enables the maintenance of the licence, thereby preventing a ‘trust deficit’ with external stakeholders (PwC, 2013). This CSR provision offers a mechanism through which businesses can create social impacts. Consequently CSR ceases to be a charitable activity, constitutes social responsibility and accords rights to stakeholders from whom the companies derive resource benefits (Kandathil and Turaga, 2014).

Although the question as to whether CSR should or should not be mandated can generate an interesting and perhaps animated philosophical debate, the introduction of Section 135 has made it a moot point. The rest of this paper discusses some of the issues and challenges associated with its implementation.

3 Issues and challenges

It is reasonable to expect a newly developed provision to require clarification, and Section 135 is no exception. Additional circulars and clarifications have been issued by the Ministry of Corporate Affairs (MCA). Regardless, there are a number of issues that are worthy of discussion. More importantly, this discussion may offer useful lessons to other developing countries that may be contemplating a move towards mandating CSR.

At the GSCSR in 2015 (see note 1 below) the Director General and Chief Executive Officer of the Indian Institute of Corporate Affairs, and a chief architect of Section 135, remarked that CSR is not about outputs but about outcomes in terms of meaningful social development within the country. Additionally, he noted that companies must exert a systematic effort rather than implementing ‘one-off’ or ‘intermittent’ projects. However, what may be missing is a broad set of desired national-level developmental outcomes that could then be more specifically defined at regional and local levels. Developing such a set of the desired outcomes at different levels can provide a good starting point for companies to plan their CSR activities.

Second, the areas of CSR activity listed under Schedule VII are not mutually exclusive. For example ‘women empowerment’ is a broad focus area which may include education, gender equity and health. India CSR Outlook Report (2016) reports that 89 companies have invested in projects supporting women empowerment and that another 229 and 219 companies respectively have invested in education and skill development, as well as poverty alleviation, healthcare and sanitation, all of which are interconnected and have a significant bearing on women’s well-being and growth. Moreover there is a lack of clarity on whether the areas listed are prescriptive or restrictive. Does the list intend to convey the message that only scheduled activities will be considered for the purpose of CSR? If not, what other social avenues being pursued by companies will be allowed as a part of CSR activities? These are especially important to clarify because the global trend in terms of responsible business is to focus equally on workplace, environment, community, marketplace, and value and transparency (Porter and Kramer, 2011).

Third, the act clearly states that activities undertaken in pursuit of the normal course of business of a company will not be considered as CSR for the purposes of compliance. This may pose a problem for some organisations. For instance ‘priority sector lending’
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could be considered as a CSR activity within the banking industry (Rai and Bansal, 2014). Priority sector lending includes making funds available for agriculture and allied activities, loans to small scale industries, small business/service enterprises, micro credit, education and housing loans and lending to weaker sections of society such as small and marginal farmers, artisans, schedules castes and scheduled tribes, and women (several of these are areas listed under Schedule VII of Section 135). The total outstanding amount of priority sector lending by the public sector banks in India, as of 30 June 2015, was approximately ₹1,771,767 crores (https://data.gov.in/catalog/bank-wise-lending-minorities-under-priority-sector-lending). However, because lending is a bank’s core activity, priority sector lending may not be counted as a CSR activity for the purposes of compliance with Section 135 thereby leading banks to think twice and undertake a serious cost-benefit exercise to evaluate the benefits associated with priority sector lending. A potential consequence of such an action is that a large portion of the population can be significantly disadvantaged.

Fourth, the act stipulates that companies must engage in CSR activities that exclusively benefit external stakeholders. This stipulation appears to contradict the World Business Council for Sustainable Development (WBCSD) which defines CSR as “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 community and society at large” [Holme and Watts, (2000), p.6]. The new section’s specific requirement of the beneficiary group is likely to disadvantage employees because many companies currently invest in CSR activities that also benefit employees (e.g., health and education). For example carpet maker Jaipur Rugs offers many programs to its weavers in the areas of financial literacy, basic hygiene and other alternative education programs through its foundation (Kalagnanam et al., 2016). Taking this away may lead to employee dissatisfaction which, in turn, may affect productivity and employee turnover. An exception is the new CSR guidelines for central public sector enterprises that allow companies to extend the benefits of their CSR projects to their employees as long as the employee group does not exceed 25% of the total number of beneficiaries of the said project.

The fifth issue is one of location. The act provides that a company should give preference to the local area in which it operates for CSR spending. This provision creates at least two problems. First, the interpretation of the term ‘local area’ may vary across companies. For example some companies may interpret it as the area within a certain radius (say 50 kilometres), whereas other companies may interpret the term from the perspective of a territory (e.g., city/district/state/region). Second it is also unclear as to how this will be implemented when a company operates out of multiple locations (Vaidyanathan and Thacker, 2014). The key question is whether a company will be allowed to choose where it will locate its CSR activities or will it be obligated to distribute its CSR budget across multiple locations. One negative outcome of requiring distribution across multiple locations is the dilution of the CSR effort.

Another potential undesirable outcome of implementing this provision is that it may actually augment rather than reduce regional disparities (Rossow, 2015). Currently seven states in India host the headquarters of ET250 companies which, taken together, will generate the highest share of CSR spending. In contrast, some other states host the headquarters of the least number of companies but are much more afflicted by social inequalities. A case in point is the India CSR Outlook Report (2016) which informs us that Maharashtra (1,105) Gujarat (711) and Tamil Nadu (625) – hardly the needy states –
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got the highest number of CSR projects while relatively worse-off states like Uttar Pradesh and West Bengal got only 472 and 467 respectively. Rossow (2015) draws our attention to the fact that a majority of the people who could benefit from CSR investment in the target areas of eradicating hunger and poverty, combating diseases and child mortality, education and gender equality are concentrated in the less developed states with a lower number of industries and hence will be deprived of this new source of funds. Further, he points out that the act seems to have missed spelling out the area of operation for new age e-commerce, Television and Broadcasting companies that have modest offices in few locations yet have a pan-India reach. In which regions should such companies be investing their CSR monies?

The sixth issue pertains to the exclusion of contributions directly or indirectly made to a political party from the scope of CSR activity (Vaidyanathan and Thacker, 2014). Although this is the right move, the Act is silent on contributions made to partner institutions affiliated with one or more politicians, or those located in a constituency represented by a politician. Would that not amount to favour for benefits in return? What about activities/institutions being run under the trusteeship or office of a politician? These are grey areas with ample scope for misuse. According to Sawhney et al. (2014) subsidiaries of US companies or those that ‘touch’ the UK have to be extra careful when choosing NGOs as partners to ensure that they do not violate the Foreign Corrupt Practices Act (FCPA) or the United Kingdom Bribery Act (UKBA). A related (political) issue is that the Act allows companies to use their CSR funds to support development projects initiated by the Prime Minister or Central Government. Additionally, the 2015 federal budget allows 100% tax exemption for contributions to selected national projects and contributions to Prime Minister’s National Relief Fund. Although some of these national projects can have significant environmental impacts if implemented properly, the proposed tax exemptions could become vehicles for political patronage, and be used as indirect political payoffs. It is worth noting here that India Inc. has been demanding that CSR spending be allowed as deduction or weighted deduction for the purpose of computing tax liability, a request that has not been conceded yet.

A seventh issue is one of continuity. The criteria in the act are based on annual figures of turnover, net worth or net profit. This means that some companies may meet the criteria in some years but not continuously over significant periods of time. However, developmental projects are usually long-term in nature spanning multiple years. The lack of continuity may steer some companies to choose small-scale projects rather than those that will lead to significant outcomes. Such behaviour is hardly desirable when sustainable social development is the goal of Section 135.

A final issue is that the Act, in its current version, does not have any coercive provisions against defaulting companies. The only expectation is that a report must be submitted explaining the reason for failure to spend the prescribed amount for CSR activities. What kinds of reasons will be acceptable is not known; similarly not known is whether this gap will be addressed in the future. Also not known is how many years at a stretch a company can default. While some companies may take advantage of the situation some others may recognise the potential risks of non-compliance as local advocacy groups can draw the attention of their failures through social media and other means. Such pressure might compel them to not default; however this is an open question. Surely ensuring compliance is going to be difficult, yet important. There is a move by the government to put in place a mechanism for monitoring CSR performance. To this end, a high level committee has been constituted by the MCA to suggest measures
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for improved monitoring of the implementation of CSR policies by the companies under Section 135 of the Companies Act, 2013. Ratan Tata, Chairman Emeritus of the prominent Tata Group of Companies, recently emphasised the need for guidelines to monitor spending of CSR funds by corporations to prevent companies from ‘wasting money’ or ‘siphoning it off’ for other activities (http://www.dnaindia.com/money/report-ratan-tata-calls-for-guidelines-to-monitor-spending-of-csr-by-corporates-2097476).

Regardless of the ambiguities, issues and challenges, Section 135 is now law and must be adhered to. It is consequently important to recognise the implications of the section both for the companies and their prospective partners, i.e., NGOs. There are several implications of the new guidelines that are worthy of consideration; these implications are for companies that will invest their financial resources in CSR projects and for the NGOs that will partner with the companies to implement the projects and are discussed in the remainder of this paper.

4 Implementation challenges for companies

There are at least four implications for companies. The first implication is capacity building within companies which begins with establishing a CSR committee; this requires companies to identify individuals competent to be part of the committee (especially those that are knowledgeable about the social sector). Section 135 requires every company, including private companies that qualify, to appoint a CSR committee of three directors of which one must be an independent director. This led to a confusion among private companies (Srivats, 2013) because the Companies Act’s (2013) provisions regarding the appointment of independent directors to a company’s board applies only to listed companies and public companies, and not to private companies. A later clarification provided by the authorities relaxed the requirement of an independent director on the CSR committee for private companies.

Realising that investors are paying increasing attention to corporate governance practices, companies are under pressure to appoint independent directors who will act as watchdogs to ensure better governance. The Companies Act (2013), for the first time, lays down specific criteria for an independent director. He (or she) must be a person who does not have any interest in the company or its affiliates and cannot have any interest with the promoters directly or indirectly (Katarki and Gupta, 2015). The subjective elements of the criteria include being a ‘person of integrity’ and possessing ‘relevant expertise and experience’. These criteria will likely narrow down the list of qualified and desirable candidates who can be appointed as independent directors. Additionally, the Act has introduced other restrictions regarding the appointment of directors such as the requirement of at least one woman director, the proportion of independent directors, liability of independent directors, reappointment of independent directors, disclosure of interest by directors, and a databank of independent directors. According to a report prepared by PwC India (2013), some of the provisions contradict regulations imposed by other regulatory bodies. Consequently the appointment of independent directors will be a challenge for a number of companies. According to Bhattacharya (2016), several companies now use consulting firms and head hunters to identify eligible, credible and truly independent persons to fill up the positions, looking beyond ‘old boys’ networks and relatives. One noteworthy feature is that the Act prohibits the appointment of service providers such as accountants and legal professionals as independent directors and also
lays down a maximum number of directorships an individual may simultaneously hold. These criteria will further narrow down the list of qualified and desirable candidates who can be appointed as independent directors, thereby limiting the ability of companies to establish a CSR committee in accordance with the provisions of Section 135.

The second implication is the need to develop a comprehensive CSR policy. A policy document will ideally contain the company’s mission and vision specifically related to the company’s CSR agenda, a plan outlining the strategic focus, criteria for selecting CSR activities, as well as operating guidelines. These are especially important to ensure that companies undertake activities that not only comply with the list in Schedule VII but also lead to a meaningful change along the social dimension. Currently many companies may not have clear cut statutory guidelines or policy directives to give a definitive direction to their CSR initiatives; this deficiency may largely be due to the “differing motivations for corporations to undertake initiatives compared to the expected benefits that they hope to derive” (Hussain, 2014).

The lack of a clear policy can easily translate into several companies being unprepared to fulfil the stipulated 2% spending in the first few years as indicated by two recent studies (Chandra and Kaur, 2015; Rana and Majmudar, 2014). Perhaps it was this concern that prompted the government to not include a penalty clause for being unable to spend the 2%. The absence of a clear policy direction as well as inadequate organisational capability to undertake substantial programs may be a reason why it has been observed that many companies have only made token gestures towards CSR such as offering donations to charitable trusts or NGOs, sponsorship of events, etc. A lack of adequate personnel to manage CSR, for example, led Coal India to announce in March 2013 that it will hire 120 personnel specifically to work on its CSR projects after it was called out for spending barely 15% of its required budget in the prior year (Sengupta, 2014). The scenario is not very different in other public sector organisations; according to the Comptroller and Auditor General, 41 central public sector enterprises failed to spend the allocated amount from 2012–2013 (Francis, 2014).

Third, companies deciding to partner with NGOs to implement their CSR plans must identify and select the right organisation to work with. Companies will need to develop clear guidelines, and perform their due diligence using pre-determined criteria, to identify suitable NGOs to implement the CSR activities. According to a government study, India has possibly the largest number of active non-governmental, not-for-profit organisations in the world (Shukla, 2010). With 3.3 million NGOs in 2009, India has one NGO for every 400 Indians and this number is many times the number of primary schools and primary health centres in India. Yet many of them have very little actual work to showcase. In such a scenario, it can be challenging for companies to choose a reliable partner. It therefore comes as no surprise that only about 30% of the top 300 firms in India work with NGOs to fulfil their CSR obligations (Rai and Bansal, 2014). To add to the difficulty in working with NGOs, many companies with foreign shareholdings are confronted with a lack of clarity around their contributions to NGOs to implement their CSR activities due to the restrictions imposed by the Foreign Contributions Regulation Act (FCRA) 2010, as well as the increased scrutiny of foreign-funded NGOs.

“As the ministry of Home Affairs tightens the noose on FCRA compliance this year, NGOs might not be the only victims of the law’s blurriness and inherent suspicion of any foreign source of funds. Companies with large foreign shareholding may also suffer, and in turn the social development work many communities count on them to fund. The Companies Act may mandate social
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A pragmatic approach in building a robust CSR agenda is therefore to make it sustainable through employee involvement (Vaidyanathan and Thacker, 2014). This entails the principles of social responsibility being incorporated into the business strategy of the company. An essential contributor to the success of CSR efforts in any company is the extent to which its employees are aware about ethical business practices and principles, so as to get their buy-in into the CSR plan. Such efforts have dual benefits: not only will employees appreciate and value the intentions and contributions of the management but will likely feel encouraged to be an important part of it through employee-driven efforts. For example, Cognizant Technology Ltd. has a very successful corporate volunteering program, Outreach (Jayashankar et al., 2013). Since its inception, over 20,000 employees have cumulatively volunteered 200,000 hours for Outreach. This is an example of a bottom-up approach with employees taking the initiative to for example, identify needy schools and the intervention they would offer. The company’s role is limited to facilitating volunteering through administrative support and a small budget. Whether employee-driven CSR qualifies in terms of complying with Section 135 is perhaps unclear. Additionally, involving employees may pose the challenge of determining how to allocate a portion of the employee cost towards CSR. In this context, it may be highlighted that the Department of Public Enterprises guidelines (Department of Public Enterprises, 2010) recommend that if a CSR and sustainability activity is closely aligned with the business strategy of a company and if the company possesses core competence to implement it in-house, then the enterprise may do so with its employees. However, monitoring of such projects must be undertaken by an external agency for the sake of objectivity and transparency.

Fourth, companies must develop reporting mechanisms that will enable them to comply with the required reporting as prescribed in the section. Several important aspects underlie accurate reporting:

1. a good understanding of the reporting requirements
2. ability to identify and track the resources consumed for the purposes of CSR and assign a monetary value to the resources
3. understanding which resources qualify to be included as valid CSR expenses and which do not (e.g., if employees volunteer a portion of their time, can a portion of their salary and benefits be allocated towards CSR)
4. internal audit of CSR activities and expenses (this would be useful as part of a due diligence process and also helpful in establishing the credibility of the company’s CSR claims).

A recently published frequently asked questions (FAQs) document prepared by the Institute of Chartered Accountants of India (ICAI, n.d.) provides some guidelines to companies on the accounting side. This includes providing clarity on the treatment of expenses as CSR expenses or those incurred in the course of regular business, disclosed or committed but not incurred CSR spends classification of expenditures as assets or expenses, and other such accounting matters. Despite these FAQs it is reasonable to expect that many companies will likely find the accounting to be confusing at least in the first few years. As an example the Act allows companies to spend no more than 5% of
their annual CSR outlay on administrative expenses. However what qualifies as administrative expenses is unclear. Moreover, 5% may be grossly insufficient especially in the first three to five years or even on an annual basis, especially for companies whose net profit is ₹5 crores. For such companies the minimum CSR outlay is ₹1 million (2% of ₹5 crores) and 5% of this amount is ₹50,000 which will be woefully inadequate.

Finally companies that desire to generate meaningful impact through their CSR activities will likely want to measure social impact, which may be defined as “… the consequences to human populations of any public or private actions that alter the way in which people live, work, play, relate to one another, organize to meet their needs and generally cope as members of society” (TICGPSIA, 1994). However, social impact is a long-term outcome which first and foremost means that a company desiring this must commit long-term funds to its CSR initiatives. Measuring social impact requires a good understanding of the nature of outcomes desired, differentiating between outputs, outcomes and impacts, a structured approach to measuring the outputs, outcomes and impacts and a sincere attempt to quantify and monetise them to the extent possible. Knowing what the desired outcomes are also helps in deciding the nature of the interventions (or CSR activities) to be implemented (this relates back to one of the early steps of CSR planning). It is also possible that certain interventions may lead to unexpected/undesirable outcomes; measuring these is also important to be able to make changes as may be necessary. Multiple approaches exist to measure social impact, and some level of consistency is required in terms of which framework(s) may be used. Moreover, measuring social impact can be a costly exercise and therefore not something that individual companies may undertake.

In a nutshell many companies, especially those with little or no previous experience with CSR, will likely face challenges right from planning through to implementation, monitoring, measurement and reporting. It would be useful for the government and/or other national bodies to develop and provide support mechanisms to such companies. These mechanisms may include research to identify developmental needs, establishing broad objectives, NGO accreditation (work has already begun on this), CSR audit/assurance guidelines and impact measurement guidelines.

5 Implementation challenges for NGOs

The amendment to the companies Act has brought cheer to several NGOs and these organisations have spent the last three years gearing up for higher levels of operation. For example CARE has been preparing by building internal capacity, hiring additional staff and working on strategies to attract more private sector projects (Francis, 2014). The process of building internal capacity requires consistent effort over a period of time and even beginning the process has not been without hurdles.

The main challenge for any NGO is the availability of qualified and willing personnel (Sundar, 2014). The 2011 census data shows that younger people (between 20 and 44 years) comprise 36% of the Indian population, which indicates the existence and potential availability of prospective employees. However, whether these individuals are qualified and willing to work in the NGO sector is an open question. Anecdotal evidence suggests that many business programs have started to introduce concepts of social responsibility to their students, and this may motivate at least a fraction of the students to consider the social sector as a possible employer. Additionally several critical factors
must be considered to develop a talented pool of qualified personnel. Although many individuals in the past may have chosen to work in NGOs as a ‘matter of calling’ and because they believed in contributing to a cause, this may not hold in the future for at least two reasons. One is the potential number of personnel required in this sector due to the Act and the other is that although many younger individuals relate to social causes, their expectations in terms of compensation, work-life balance and other employment-related expectations may be different from what NGOs can offer.

One of the key challenges in attracting the right kind of talent into this space is the absence of a professional work culture. Professionals who want to build a career will generally look for a favourable work environment, one that promotes cooperation, fairness and meritocracy. The NGO sector may still not be an obvious choice for professionals, but anecdotal evidence suggests that positive change and the satisfaction of helping out weaker sections of society emerge as drivers of interest in this sector among the younger generation. By bringing in qualified outsiders, redesigning organisational structures, and introducing a more disciplined and professional work ethic, NGOs can significantly alter their institutional culture. Further, since employee commitment and belief in the cause are central to an NGO’s effectiveness, instilling the values espoused by the organisation among employees is imperative for maintaining reputation and establishing trust among clients and beneficiaries. For this reason, NGOs must contemplate as to how a prospective employee’s individual aspirations and the organisation’s values can be aligned. As Herzberg et al. (1959) noted decades ago, basic pay and office environment can only be hygiene factors and are therefore limited in their role to attract a prospective employee. Motivating factors such as creative work, sense of accomplishment, responsibility and growth opportunities, respect and recognition must be highlighted for attracting and retaining worthy employees. NGO employees must transform into becoming ambassadors of the cause they espouse and live their organisational values. Having such individuals can significantly enhance an NGO’s reputation.

On the talent front, if there has to be a consistent and sustainable improvement in the number of individuals who see a career for themselves with NGOs, then it is imperative to have leadership development programs to identify and groom future leaders of the social sector. This need for education in management and leadership is accentuated by the fact that NGOs cannot afford to hire consultants and change management experts to address their growth challenges. These have to be internally driven and managed. Such developmental programs for NGO personnel are just beginning to be integrated into the curricula of management institutions in India.

The final aspect pertains to the retention of employees, particularly because the social sector is growing. With CSR becoming mandatory, several NGOs are considering scaling up their operations to benefit from the tide of opportunities that are now hitting their shores (Francis, 2014). This, in a way, will worsen the problem of staff retention because a greater number of opportunities could result in greater movement of personnel across NGOs, at least in the foreseeable future.

A second challenge is on the strategic side especially in the case of newer NGOs that are likely to face significant growth in a short time-frame. Organisations must undertake the exercise of clarifying their mission and vision and establish policies, strategies and guidelines to run the organisation. One outcome of such an exercise is that it provides a roadmap to NGOs to think about the developmental areas that they will focus on. In turn this will help them determine which types of projects they will accept and which ones...
they will not (note: smaller NGOs may not have too many choices). Another outcome of such an exercise is that it helps NGOs establish operating guidelines and procedures, which are essential when an organisation experiences growth.

The third challenge, following from above, is one of governance, management control and operational control. Regardless of whether an NGO is registered as a trust, society or a Section 8 company, it is expected to maintain a basic governance structure (PwC, 2013). Establishing a strong governance mechanism is critical to ensure smooth functioning of the organisation both from an operational side and the financial side (especially to avoid fraudulent activities). This may include developing:

1. a formal organisational structure so as to clarify communication channels and establish accountability patterns
2. formal policy manuals with respect to human resource management, finance and accounting (including budgeting, cash management and internal controls), purchasing and other operating guidelines (including standard operating procedures and decision making criteria)
3. performance criteria to assess performance at the individual, project and organisational level
4. mechanisms to address the reporting requirements of various stakeholder groups.

Attention to record-keeping and performance measurement (including social impact measurement) is especially important because contributing companies will require this information for their own reporting and will rely heavily upon the NGOs to furnish such data. The focus on accountability will increase significantly.

In the current scenario, marketing and branding exercises are the need of the hour for NGOs to create visibility among companies so to enable them access company funds. In a way, the mandatory CSR has brought to the fore a paradox of sorts. On the one hand, we have several NGOs vying for funds while several companies that are keen to invest their profit into CSR are unable to choose among the various NGOs or know which ones are credible enough to partner with. Companies are now approaching consulting organisations like Ernst and Young who offer advisory services that include development of CSR policy and a roadmap to operationalise it as well as help build a monitoring mechanism to ensure implementation of plans. Organisations like the Indian Institute for Corporate Affairs (IICA) and the Tata Institute of Social Sciences (TISS) have been tasked with the responsibility of creating ‘CSR hubs’ to facilitate the companies and NGOs to connect with each other (Francis, 2014). The hub carries out activities in a partnership mode i.e., TISS, civil society organisations, and the concerned Public Sector Enterprises, and offers capacity building, and advocacy services. Additionally, several prominent private consulting companies such as CSO Partners, Soul Ace, I ImpactIndia and Indian Centre for CSR (ICCSR) offer help with the implementation process.

Regardless, there is potential for bridge organisations to emerge that can connect companies with the financial resources and NGO partners. Such a win-win arrangement currently seems farfetched with 34% of the top 300 Indian firms working through their own foundations and trusts (Rai and Bansal, 2014) rather than with NGOs.

Finally, with companies having to explain their CSR spending and assess the impact of their expenditure, the need for accrediting NGOs that will be the implementation
partners is being felt acutely. CRISIL, India’s leading rating agency has recently evolved
an NGO-specific evaluation process for accreditation. NGOs will now be accredited
based on their performance and financial proficiency. The objective is to assess
an individual NGO’s capacity to deliver based on its profile, process and programs. The
accreditation process will also verify training of field staff or a grievance mechanism for
beneficiaries and lastly conduct an impact analysis of flagship programs (Kably, 2014).

Although the NGOs face many challenges, these are not insurmountable. In fact the
CSR scenario provides an opportunity to the larger and more established NGOs, as well
as some of the large foundations established by companies, to mentor the smaller ones in
an effort to share the social development responsibility. This, of course, requires an
attitudinal shift among the larger NGOs and foundations.

6 Conclusions

The introduction of Section 135 in the Companies Act (2013) has wide-ranging
implications for the nation’s social, environmental and economic development. This
research note outlines the implications of the provisions of the section and the
implementation challenges faced by companies and NGOs. The paper notes that many
provisions within the section still require clarifications, and both companies and NGOs
could benefit from support mechanisms to enable more effective and efficient compliance
by companies. The introduction of this section provides significant opportunity for
academics and practitioners to conduct empirical research in order to examine, analyse
and understand practice as the country takes stock of the early years of its
implementation. Future research may include small and large scale surveys to better
understand the lay of the land with respect to CSR compliance and implementation, and
detailed case studies of companies and NGOs (either independently or as a pair of partner
organisations) to better understand compliance and implementation challenges.

India’s experience with the nationwide implementation of mandatory CSR may
provide the impetus to other governments around the world, especially in developing
countries, to consider something similar. This would be similar in spirit to developments
in one or two countries spreading to other parts of the world like the ‘Norwegian gender
quota which is now being emulated by many other countries around the world’3. The
provisions of Section 135 may offer some lessons for the mandatory CSR in Indonesia,
which requires limited liability companies that are related to the field of natural
resources. These companies are required to budget for CSR activities which will be “…
implemented as a joint venture between the state, employers and the public, especially
the surrounding communities …” [Arjaya et al., (2014), p.4]. One such lesson may be the
requirement for a minimum allocation, the other may be the kinds of activities that
qualify for CSR, and a third lesson may be the reporting and monitoring of such
activities.

A more interesting question down the road pertains to the outcomes and benefits
derived from mandating CSR both for companies that are required to comply with
Section 135, as well as the stakeholder groups that are supposedly the beneficiaries of an
individual company’s CSR activities. In conclusion a mandatory CSR regime has the
potential to raise many interesting questions, as well as to contribute to the nation’s social
development agenda in a meaningful way.
References


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Sundar, P. (2014) CSR and the Companies Act: Challenges as Opportunities [online] https://www.academia.edu/22635186/CSR_and_the_Companies_Act_Challenges_As_Opportunities (accessed 12 May 2016).


Notes
2. ₹ is the currency symbol for the Indian Rupee; one crore = ten million. The prevailing exchange rate on 11 January 2017 was 1 = U.S. $0.01465 (http://www.bankofcanada.ca/rates/exchange/daily-converter/).
3. We thank an anonymous reviewer for this suggestion.