CSR's sub-par reputation

India's unique corporate social responsibility (CSR) law was introduced in 2013 under the second United Progressive Alliance government at a time when India Inc's reputation was somewhat tarnished. Anil Agarwal's Vedanta was embroiled in a controversy over mining bauxite in a tribal area in Odisha. The famous "no-go area" dispute over allowing or disallowing coal mining in environmentally fragile forests in the east had erupted within the government under pressure from the mining lobby.

The government's optimistic special economic zone (SEZ) policy of 2005 provoked a rash of indiscriminate land acquisition that often defrauded farmers and land losers of rightful compensation. These devious practices prompted the passage of a land acquisition law that made it well-nigh impossible for corporations to acquire land. The Satyam scandal had broken out in all its fraudulent ignominy, raising questions about the legitimacy of independent directors and casting a shadow over India's fabled "IT story". Prime Minister Manmohan Singh's mild suggestion that chief executive officers should pay themselves less in the interests of equity sent C-suites into a tizzy.

SWOT

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So the move to make CSR spending compulsory was seen as a policy corrective to corporate excess and hinted accusations of cronyism. The mandate under section 135 of the Companies Act for listed companies of a specified net worth, turnover, and profitability was designed to remind corporations of an obligation to society at large. Eligible companies must spend at least 2 per cent of their average net profit over the previous three financial years on CSR activities. Those that do not do so must explain why. Specifying the areas that qualify for CSR activity also aligned corporate philanthropy to the government's socio-economic policies — health, education and so on.

On the broad philosophical principle of "do no harm," the policy has worked. CSR spending has grown strongly — in FY24 alone, spending by listed companies rose 16 per cent to ₹17,967 crore. According to Prime Database, 98 per cent of companies met their CSR obligations and about half went beyond the required spending. The latter fact is notable because CSR spending cannot be deducted from taxable income unless the money is being donated to organisations that have tax-exempt status. With foreign funding for NGOs becoming increasingly problematic, domestic CSR money has admittedly become a critical source of funding for thousands of voluntary organisations working at the grassroots. The policy has the additional benefit of getting corporate executives out of their air-conditioned cocoons into the real world of Bharat.

But as a strategy to transform India's socio-economic dynamics, the gains from the CSR mandate are less evident. In recent years, studies have shown that the relatively economically prosperous states — Maharashtra, Rajasthan and Tamil Nadu, where most companies are located — are the ones that have been the prime beneficiaries of CSR funding. According to the latest one by Development Intelligence Unit, districts in six zones that the NITI Aayog had labelled as "aspirational" (meaning low income) — Jharkhand, Chhattisgarh, Bihar, Odisha, Madhya Pradesh and the Northeast — receive less than 20 per cent of the total CSR pool.

Most of the money, researchers in multiple institutions have found, goes into high-profile sectors such as education and healthcare. Slum development, livelihood enhancement and environmental projects get far less attention, though they too are hot-button issues. Though it would be unfair to label CSR as compliance-driven virtue signalling, it is also true that companies are likely to invest in areas beyond their immediate ambit and in causes that ensure maximum PR bang for the buck.

The additional problem with legally mandated CSR spending is the opportunity it affords for increasing government intrusion. In a throwback to the licence raj era, the law already tells companies how much to spend and what they can spend it on. It is not outside the realm of possibility that the discovery of the skewed geographical nature of CSR spending would prompt the government to stipulate region-wise targets next. The legal obligation creates additional headaches. In 2018, for instance, the government issued preliminary notices to 272 companies for not complying with their CSR obligations.

India is the only country to have a legal mandate for CSR (under section 135 of the Companies Act). Most other countries such as the United States, the United Kingdom and the European Union follow policies designed to nudge companies to follow CSR programmes. Critically, most of these jurisdictions have inheritance taxes, the major reason billionaires such as Bill Gates and George Soros set up massive charitable foundations in their lifetimes. India scrapped its version of inheritance tax in 1985 because the collections were meagre and the cost of collection high. In the West, however, this tax has unleashed enormous sums of money for social causes that have made an appreciable impact on a range of issues.

Despite the creation of a powerful industry-CSR complex as a result of the new-found ideal of CSR, the biggest irony is this: In public perception, whatever the magnitude of spending wherever in the world, corporate reputational values, whether in India or globally, still trade well below par.