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# Corporate Social Responsibility and Factors Influencing it

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## ABSTRACT

*Corporate Social responsibility can be said to be a post-world war II phenomenon because that is when the philanthropy about business ethics began to be developed, and there was a lot of awareness within the public as well as the government because ultimately it was for the welfare of the people. This idea usually rests on a give and take concept. The Corporation takes resources from people hence it deserves to compensate the people. The origin and the development of this concept or rather the reason that the corporation should do work that benefits the society at large can be understood from the various theories about corporation such as artificial entity theory, real entity theory, and aggregate theory, which would be understood along with various theories of Corporate Social Responsibility. Since this whole policy is very nascent in the country there a few known factors that affect the implementation as well as the success rate of these policies. Issues such as transparency and lack of consensus over activities plague the corporates. The community as a whole also fails to participate in these activities mostly because of unawareness. Civil societies, if they are stronger in the Nation would aid in the strengthening of these policies and their application. Also factors such as management support, financial assistance and government as well as physical environment, stakeholder values, company's internal policy, ethical practices and the probability views in relation to Corporate social responsibility and its implementation. The paper would look in the CSR committee policymaking and their implementations.*

## I. INTRODUCTION

Corporate Social responsibility is a concept and philosophy that has developed the latter half of the 20<sup>th</sup> century. "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 the local community and society at large."<sup>2</sup> . The word 'corporation' is actually derived from the Latin word 'corpus' which

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<sup>2</sup>Samuel O. Idowu, 'World Business Council for Sustainable Development' [2013] Encyclopaedia of Corporate Social Responsibility.

means ‘a body of the people’ and under the ancient Roman Law, these bodies “ had a strong social aspect to them and were often organized for social purposes, such as asylums, homes for the poor, homes for the aged, hospitals, orphanages, political clubs and burial societies.”<sup>3</sup>

One of the earliest cases wherein a company wanted to carry out activities that would benefit the masses was by Mr. Henry Ford and he even was sued by the people who did not want him to carry out this philanthropic work. This judgement forced him to drop his charitable work and instead run the company for profits as the court declared that “for-profit corporations must be run to produce a profit.”<sup>4</sup> This was a wrong precedent and was rejected by many states. This was later questioned and mostly rejected by the courts as time passed. As time passed different people came up with different ways to approach Corporate social responsibility, three of them can be considered as the main theories, Carrols four-part model, the triple bottom line and the stakeholder approach.

This concept is rather very new for the Indian subcontinent. It was in the year 2013 that the “Companies Act, 2013” was approved by the parliament. In this act a lot of new concepts were introduced to keep up with the international scenario and one of the concepts was that of “Corporate Social responsibility”. Under Section 135 of this act, it was stated that wherein a company that has a turnover more than a certain limit prescribed by the act shall establish a Corporate social responsibility committee. This committee will also decide the amount of money to be spent on activities and monitor the execution of the activities. The list of activities has been given under Schedule VII of the act itself. The section was supplied with various subsections and provisions to those subsections which would be dealt in detail in the paper. Along with the act new notification was released in the year 2014 by the Corporate Affairs Ministry. It allowed for the creation of “Companies (Corporate Social Responsibility Policy) Rules, 2014.” The rules were essential in guiding the companies as to how to approach this new committee inside its internal working and the procedures that were to be followed by the internal Corporate Social Responsibility committees. In other words, it was an essential guideline for the Corporates to follow as this was the first time such a policy was being introduced in the country. This paper would look into the development of CSR along with the factors that influence its development.

## II. DEVELOPMENT OF CORPORATE SOCIAL RESPONSIBILITY

The origin to a socially, morally and ethical responsibility which the corporations owe to the

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<sup>3</sup>Harold J. Berman, *Law and Revolution: The Formation of The Western Legal Tradition* (1st ed., Harvard University Press 1983).

<sup>4</sup>*Dodge v Ford Motor Co* [1919] Supreme Court of Michigan, 170 NW (Supreme Court of Michigan).

community and society at large can only be well comprehended by understanding the prevalent theories of Corporations. They very well underline the requirement of Corporate Social Responsibility. The Three prevalent theories of “Corporations are the Artificial entity theory, real entity theory and Aggregate theory.”<sup>5</sup>

The artificial entity theory proclaims that the corporations are actually big artificial entities and they exist because of the government practices.<sup>6</sup> This theory is sometimes referred to as concession theory as well. This theory states that the corporation is separate from the government and from the people that run it. It is an entire being on its own. However, it also states that it exists only because of the acts of the government, implying that the government has provided these corporations special privileges and it is because of those privileges that it exists. Hence, justifying the other name i.e. concession theory. Thus because of these concessions the government has the authority to control and monitor these corporations. It was first referred to in the case of “*Trustees of Dartmouth college v. Woodward*, wherein the Supreme Court of United States stated that, A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law.”<sup>7</sup>

The theory of real entity is somewhat similar to the artificial theory. It states that corporations tend to differ from the people who operate it and the state, but they possess their own different personality and identity which is beyond the state and the people who operate it. Some scholars have even said that corporations should be given human rights.<sup>8</sup> It is also known as the natural theory of corporations. The aggregate theory on the other hand states that the corporation is actually the “sum of the individuals that the organizing, operating and owning it.”<sup>9</sup> Thus, justifying its other name i.e. the Nexus of Contract theory. The difference between artificial, real and aggregate theory is that the former two define corporations as separate from the state and the operators while the latter theory states it as the opposite of it having no separate identity of its own.

There are three leading and popular theories of Corporate Social Responsibility, the Carroll Theory, The triple bottom line theory and the stakeholder theory. The Carroll theory defines CSR as “encompassing the economic, legal ethical and philanthropic expectations placed on

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<sup>5</sup> Strine L and Walter N, ‘Originalist or Original: The Difficulties of Reconciling *Citizens United* with Corporate Law History’ (Social Science Research Network 2016) SSRN Scholarly Paper ID 2567416 <<https://papers.ssrn.com/abstract=2567416>> accessed 19 October 2020.

<sup>6</sup> Avi-Yonah RS, ‘Corporate Taxation and Corporate Social Responsibility’ (2014) 11 NYUJL & Bus. 1.

<sup>7</sup> *Trustees of Dartmouth College v Woodward* (1819) 17 U.S 518 (Supreme Court of United States on America).

<sup>8</sup> Rubin D, ‘Corporate Personhood: How the Courts Have Employed Bogus Jurisprudence to Grant Corporations Constitutional Rights Intended for Individuals’ (2009) 28 QLR 523.

<sup>9</sup> Stewart FL, ‘The Corporation, New Governance, and the Power of the Publicization Narrative’ (2014) 21 Indiana Journal of Global Legal Studies 513.

organisations by society at a given point in time.”<sup>10</sup> There are four obligation for the corporation according to this theory. Firstly, it has an economic responsibility, i.e. the contribution to the economy of the state. There has to be a reasonable profit for the shareholders, job satisfaction as well as a well-paid job for the employees and customer satisfaction. Secondly, the legal responsibility to the uphold the various rule and regulations laid down for basic operation. Thirdly, Ethical responsibility means doing what is right and fair. This is the important obligation according to Carrol. He has said that the corporations should always do the right thing even when the law doesn’t require them to. Lastly, Philanthropic responsibility to improve the lives of other people without seeking any monetary benefit from it. To look into the welfare of the community at large.

The Triple bottom line approach is that there should be three end goals that a corporation should have as its aims. They should be profit, people and the planet.<sup>11</sup> All these three have to be not at a loss if not being benefitted. This is a way to make corporations commit of Corporate social responsibility along with helping the goal of environmental sustainability. Economically, corporations should be making profit, Socially, they should be helping and developing the community and Environmentally they should be concentrating on sustainability and minimizing global warming, wastage and using renewable resources.

The stakeholder approach is said to be the mirror image of the concept of Corporate Social Responsibility. It means that it has the same end goal but it begins from the exact opposite approach. Instead of setting up a company and then focusing on what groups would be affected by it as well as other environmental and ethical effects, stakeholders of the corporation themselves represent these issues.<sup>12</sup> The common ground for both the Stakeholder concept and the Corporate Social responsibility concept is morality and ethics.

### **III. IMPLEMENTATION: “COMPANIES ACT, 2013 AND CORPORATE SOCIAL RESPONSIBILITY RULES, 2014.”**

The newly drafted “Companies Act” in 2013 contains a mandatory provision for corporations to engage in “Corporate Social Responsibility”. Section 135 of the said act has multiple subsections explaining in detail about the applicability and extent of this responsibility. It states that if a particular corporation is “having a net worth of Rupees five hundred crore or more, or a turnover that is a thousand crore or greater than that, or having a net profit of more than

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<sup>10</sup>Carroll (n 6).

<sup>11</sup> Adrian Henriques, ‘CSR, Sustainability and the Triple Bottom Line’, *The Triple Bottom Line* (Routledge 2013).

<sup>12</sup> Brown and Forster (n 7).

five crore in the immediately preceding financial year should constitute a CSR committee.”<sup>13</sup> Any company that satisfies these three conditions has to comply with the whole provision of CSR.<sup>14</sup> Companies can be subjected to fine if discovered to have not constituted a CSR committee even if it satisfied the conditions under Section 135 (1).<sup>15</sup> However, if the company ceases to satisfy the three criteria under Section 135(1) in any financial year would be exempted from the scope of Corporate Social Responsibility which includes the winding up of the company.<sup>16</sup> If the company is a subsidiary company or a holding company then it has no compulsion to adhere to the Corporate Social Responsibility mandate. It also does not apply to a Section 8 company.

The committee shall comprise of three or more than three directors with at least one director being an Independent director. In a situation where the company does not possess the capability to appoint an independent director then the Corporate social responsibility committee shall consist of minimum two or more directors. In case of private company that only has two directors that comprise the whole board, those two directors would only constitute the Corporate Social Responsibility committee. If the company satisfies the requirements of a Foreign company then the committee would comprise of two people out of which at least one shall be a resident of India who satisfies the provision of Section 380 (1) (d).

One of the main tasks of the Corporate Social Responsibility committee is to formulate CSR policies and recommend it to the Board of directors. The acts which the company can indulge in are listed in Schedule VII of the Companies Act, 2013. The subject areas for these activities can be the promotion of a better health care system, increased hygiene of sanitation, Funding free education for impoverished children, providing better housing for those who live in a slum or down-trodden area, conduct campaign for gender equality, women rights, caste based discrimination, look into environment sustainability methods to employ in their own corporation, protect the wildlife environment, provide funds to develop and maintain a national heritage, create funds for armed sports veterans, help war widows, contribute to a government fund for relief activities and provide relief in area battling a natural calamity by donation material for construction and rehabilitation activities.<sup>17</sup>

Under the “Companies (Corporate Social Responsibility policy) rules, 2014” a company is

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<sup>13</sup> Kapoor and Dhamija (n 5).

<sup>14</sup> *Sri Balaji Shivalingam v Commissioner of Income Tax, AP, Hyderabad* [2014] SCC OnLine 1238.

<sup>15</sup> *Pan Asia Logistics India Private Limited* [2018] SCC OnLine 11589.

<sup>16</sup> *The Managing Director M/S Lvsr Famrs Pvt Ltd, Vs the Official Liquidator High Court of AP, Hyderabad and Others* (2012) 6 ALD.

<sup>17</sup> Kumar (n 8).

allowed to partner with other companies for fulfilling the social responsibility mandate. This can be done only when both the companies are complying with rules that demand the reporting of this singular activity separately by both the companies. If any CSR activity is benefiting the company or its employees, it cannot be considered as a CSR activity. The activity should also ensure that the money that is allotted for CSR activities which is “two percent of the average net profit made in the previous financial year according to section 135 (5),”<sup>18</sup> is spent in the succeeding financial year.

There are certain rules which guide the committee as well as the companies for a smoother implementation. The board always has to approve the policy proposed by the company and then only the committee can initiate those policies. The board always has to ensure that the allotted CSR funds are exhausted completely each financial year. Preference for conduction of activities should always be given to nearby and local areas. On failure of complete spending of the allotted CSR funds, the reasons should always be given in a report by the Board.

In a recent case, a certain company failed to complete its allotted CSR funds, but it provided a reason for that mistake in their annual director’s report. But on further investigation it was found that the numbers were incorrectly mentioned in the report. The tribunal ruled that the company can file a fresh report and Registrar of companies can also initiate proceedings against its directors under Section 441 of the Companies act for defaulting in their act.<sup>19</sup> In a few separate cases for not exhausting the allotted CSR budget and failing to provide a reason for the default in the directors’ annual report<sup>20</sup> and hence violation Rule 8 of the CSR rules.<sup>21</sup> The National Company Law Tribunal observed that the Registrar of company can institute proceedings under section 441 of the act for ensuring the liability of the director and other concerned officers.<sup>22</sup> . For the violation of Section 135, “an application under section 441 of the Companies act has to be filed.”<sup>23</sup> Although if the companies over spend they cannot carry over but if they under spend they can carry over to the next financial year but this amount has to be added to next financial years allotted CSR funding according to Section 135 (5). This funding can only be decided after the financial accounts for that year have been settled.<sup>24</sup> This is the only fair way to determine fair and just CSR accountability.

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<sup>18</sup> Kapoor and Dhamija (n 5).

<sup>19</sup> *Technicolor India (P) Ltd v Registrar Of Companies* (2020) 7 TMI 423 (National Company Law Tribunal).

<sup>20</sup> *Alok Pharmaceuticals and Industrial Company Private Limited* [2018] SCC OnLine NCLT 28915.

<sup>21</sup> *Rapid Estates Private Limited* [2018] SCC OnLine NCLT 545.

<sup>22</sup> *Avinash Developers Private Limited* [2018] SCC OnLine NCLT 29665.

<sup>23</sup> *Shoft Shipyard Private Limited* [2018] SCC OnLine NCLT 13576.

<sup>24</sup> *M/s Hira Power and Steels Limited*. CP No.: 2707/441/NCLT/MB/MAH/2018.

The act as well as the CSR rules are very comprehensive in nature. They list down the methods as well as the procedures for the conduction of CSR related activities. They also provide for sanctions by law if a company fails to abide by the standard, but it also gives chances to correct mistakes. To encourage companies a “National Corporate Social Responsibility award has also been instituted. So, that their fruitful efforts do not go unnoticed. To have a well-maintained data base a CSR cell was constituted under the eyes of the Ministry of Corporate Affairs. This would ensure proper working of the CSR committees of each and every qualifiable company.

#### **IV. FACTORS AFFECTING CORPORATE SOCIAL RESPONSIBILITY**

The CSR factors are affected by various obstacles. It has to be taken into account that India is indeed still a developing country and hence a lot of the CSR activities would be focused on eradicating poverty more than focusing on environment sustainability. The main factor that actually effects the implementation is collective action. India has an enormous number of companies that qualify for the constitution of a CSR committee. However, due close to zero collective action, the amount of development of the society is lessened.<sup>25</sup> These separate conglomerates work on different fields and achieve less, if they were to work towards a common goal of providing any facilities under Schedule VII, the effect and outcome of their CSR activity would be two-fold.<sup>26</sup> Another important factor as deduced by an empirical research was the difficulty to identify which area should be developed to maximize societal welfare.<sup>27</sup>

Lack of trust between the local community and the corporates also leads to lesser efficiency of the implemented policies. There is an absence of any ingenuity to integrate CSR in the local communities. This local integration would be extremely beneficial because small communities build each other and develop together. The issue of transparency also effects the implementation. The corporates do not have a very trust-based relationship with the corporates. The corporates have a hard time believing the data as well as the fund utilization practiced by the NGO's. The NGO's also do not make an effort to help corporations with these activities, they don't share their data because of which the companies are not able to assess the actual impact.

Issue of collective action once again gains importance due to the multiplicity of same kind of

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<sup>25</sup> Oliver (n 9).

<sup>26</sup> Dasaratha Rama and others, 'CSR Implementation: Developing the Capacity for Collective Action' (2009) 85 *Journal of Business Ethics* 463.

<sup>27</sup> Jessi Golda, 'Driving Factors Of Corporate Social Responsibility In Indian Companies' (2020) 7 *Journal of Critical Reviews*.

initiatives being employed and in the same subject area which leads to unhealthy and unnecessary competition between corporates. This decreases the impact of the whole object behind the introduction of a compulsory Corporate Social Responsibility Mandate. The role of civil societies in any nation is far-reaching. “Partnerships between effective corporate, NGOs and the government will place India’s social development on a faster track.”<sup>28</sup> Civil societies comprise of people from all bends of life. The partnership of Companies with civil societies would make for more stakeholders contributing to the social benefit. Civil society are mostly plagued by bad management of finances and human resources which could be solved by the companies. This would be a mutually beneficial relationship. The concentration on equity more than equality has to be inculcated in these policies.

## **V. CONCLUSION**

Corporate Social Responsibility has gained more ground since the last fifty years because the government has realised that the corporates have always been on the receiving end. Their time has come to give back to the people. A give and take relationship had to be established or the rich will keep getting richer and the poor getting poorer. India has actually fared much better than other developed countries when it comes to inclusion of Corporate Social Responsibility in our law. Thus, making it mandatory for companies to do charitable work. However, the standards for the amount also are kept varied to keep an equitable relationship between different sizes of companies. The laws and the accompanying rules are comprehensive and did not seem to possess any lacuna. Nevertheless, we can do better when it comes to the implementation of these laws. The various factors that decrease the impact of these welfare initiatives can be discussed by the law-makers and a solution can be laid down. The need for collective action is very real and if addressed at the earliest would be helpful in making a targeted action with an outcome that is very evident

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<sup>28</sup> *ibid.*