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An Analysis of Corporate Social Responsibility Expenditure in India

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The article analyses the trend of corporate social responsibility expenditure by firms in India, especially in the wake of the new Companies Act, 2013. It emphasises the relationship between CSR expenditure and profits of the firm and highlights how the firm size positively affects this relationship.

The United Nations Industrial Development Organisation (UNIDO) has defined corporate social responsibility (CSR) as

> a management concept whereby companies integrate social and environmental concerns in their business operations and interactions with their stakeholders. CSR is a way in which companies achieve a balance of economic, environmental and social imperatives.

CSR has been practiced by companies in the developed world in a big way. Most of the large private universities in the United States (US) were setup as a part of CSR activities undertaken by large corporates. A lot of multinational companies contribute towards the development of societies in which they operate. A most notable example is Shell, an Anglo-Dutch multinational oil and gas company, which supports the local communities in Nigeria. In India, large scale philanthropic activities were undertaken post-independence, which led to the setting up of some of the most prestigious institutions of professional education. Companies also contributed by making donations to non-governmental organisations (NGOs) and their own trusts, which were deductible under Section 80 G of the Income Tax (IT) Act. However, the donations were not transparent and lacked accountability.

CSR Made Mandatory

In order to streamline the philanthropic activities and ensure more accountability and

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transparency, the government of India made it mandatory for companies to undertake CSR activities under the Companies Act, 2013. The concept of CSR is defined in clause 135 of the Act, and it is applicable to companies which have an annual turnover of Rs 1,000 crore or more, or a net worth of Rs 500 crore or more, or a net profit of Rs 5 crore or more.

Under this clause, these companies are supposed to set aside at least 2% of their average profit in the last three years for CSR activities. The law has listed out a wide spectrum of activities under CSR, which cover activities 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 among others.

The companies can carry out these activities by collaborating either with a NGO, or through their own trusts and foundations or by pooling their resources with another company. The law also entails setting up of a CSR committee which shall be responsible for decisions on CSR expenditure and type of activities to be undertaken. This committee shall consist of three or more directors, with at least one independent director whose presence will ensure a certain amount of democracy and diversity in the decision-making process.

The law is very significant, because India is at the threshold of demographic dividend, and there is an urgent need for the creation of human and physical capital to reap its rewards. Investment in education, health, skill development and social infrastructure will enhance capabilities of the youth by improving their nutritional, skill and educational level, which in turn will better their employment prospects.

Traditionally, this has been the responsibility of the government, but since public delivery of goods and services has been riddled with corruption and bureaucratic inefficiency and the welfare schemes are plugged with leakages, CSR is being seen as an alternative to governmental provision of merit goods. CSR will increase availability of funds for welfare activities and may lead to delivery of goods and services to the people in a cost-effective manner. The clause on environmental sustainability will help in bringing down pollution and emission of greenhouse gases and will help in compliance with international norms and regulations. Therefore, the clause on CSR is a step towards achieving social and environmental sustainability, which will benefit society in future.

In the first section, the trend of CSR expenditure incurred by the top firms in the country in the last three years and the changes that have occurred in the wake of the enactment of the new Act have been looked at. The second section highlights the positive correlation between profits and CSR and how this relationship gets accentuated as the firm size increases. In the third section, we have detailed the types of CSR activities undertaken by various companies across ten major industries in India.

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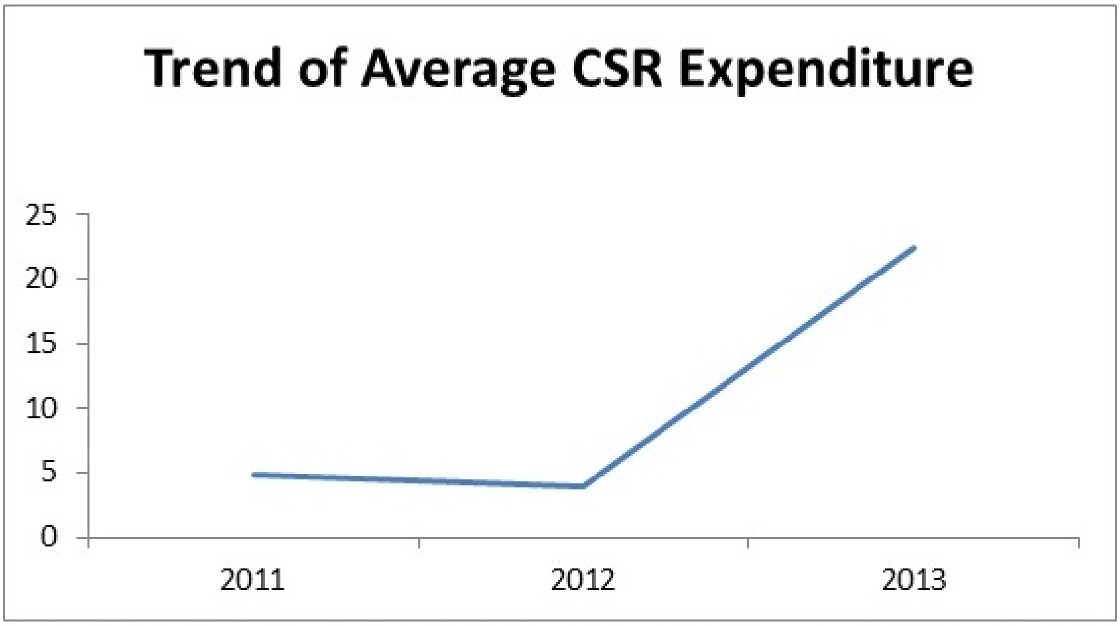
Disclosure of CSR Activities Made Compulsory

Prior to 2012-13, many firms were voluntarily making donations and spending on community development and mitigation of environmental pollution. It is only since 2012-13 that firms have started allocating funds for CSR activities specifically. This was in response to the Securities and Exchange Board of India (SEBI) circular dated August 2012, which mandated all top 100 listed companies to include business responsibility report as a part of their annual report.

Therefore the year 2012-13 marks a turning point, where we can see a marked difference in the CSR initiatives adopted by the firms. We have compared the donations made and CSR expenditure incurred by firms in the last three years, using firm level data from Prowess (Centre for Monitoring Indian Economy). Even though it was not mandatory to spend on CSR initiatives in 2012-13, there was a marked increase in the average CSR expenditure by the firms in 2012-13 in response to the passage of the Act in August 2013, as compared to the previous year.

Figure 1: Average CSR Expenditure



X-axis: Year; Y-axis: Average CSR expenditure of all firms (in million rupees)
Source: Calculated by the authors using Prowess data for the year 2012-13.

Figure 2: Trend of Average CSR Expenditure with Respect to Ownership

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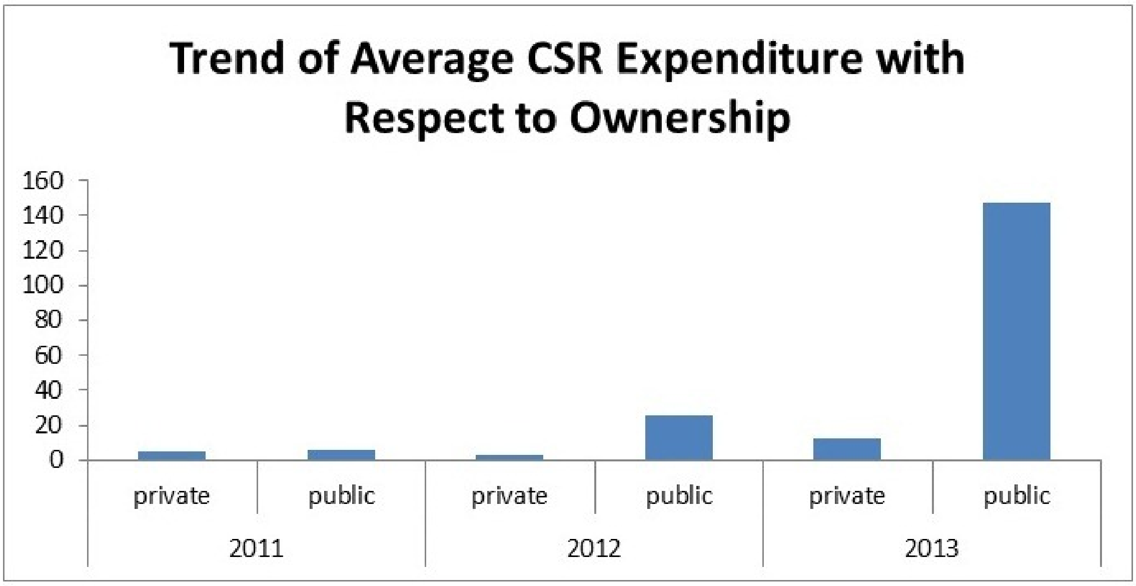

X axis: Year and Ownership; Y-axis: Average CSR expenditure (in million rupees)
Source: Calculated by the authors using Prowess data for the year 2012-13

CSR expenditure by public sector firms increased considerably in 2012-13 compared to 2011-12. The passage of the Act also led to an increase in the average CSR spending of public sector firms from Rs 25.72 million in 2012 to Rs 147 million in 2013.

Figure 3: Trend of Average CSR Expenditure with Respect to Foreign and Domestic Ownership

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X-axis: Firm ownership and Year; Y-axis: Average CSR expenditure (in million rupees)
Firms which are owned by foreign parent companies have been classified as foreign.
Source: Calculated by the authors using Prowess data for the year 2012-13.

There has also been a significant increase in the average CSR expenditure by domestic firms as compared to foreign firms. Average CSR expenditure by domestic and foreign firms was Rs 3.79 and 8.5 million respectively in 2011-12, but this increased to Rs 22.6 million and 19.5 million respectively in 2012-13. Foreign firms increased their expenditure, because they might have been driven by the need to protect their brand name. Anticipated future pressure from consumers, investors and NGOs may also have been the driving force for foreign firms to invest in socially responsible activities.

The passing of the Act also led to a steep rise in the number of firms disclosing their CSR expenditure. In 2010-11, 336 firms had disclosed their donations and expenditure on community and environment related activities. This number rose to 504 in 2011-12, and to 1,470 in 2012-13. There was an increase in environmental reporting by firms as well. In 2010-11, only 35 firms had complied with environmental reporting, while 52 had filed reports in 2011-12. But in 2012-13, there was an increase of 211.5%, with 162 firms disclosing their environmental performance information.

In 2012-13, 760 firms had crossed the threshold of Rs 5 crore net profit, but their total CSR contribution was lesser than the 2% criterion as laid down by the Act. The total CSR spending by firms was Rs 33,668 million, but the required spending should have been Rs 45,154 million.

Figure 4: Required and Actual Expenditure by Firms Meeting the Threshold

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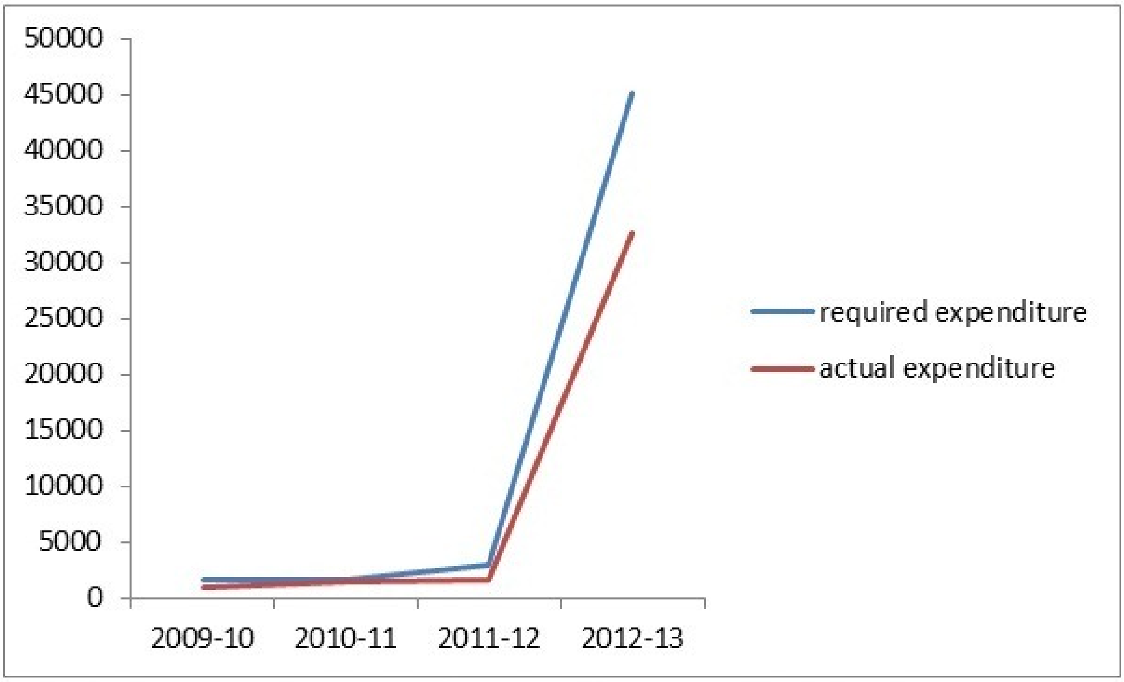

Y axis: Required and actual expenditure in million rupees; X axis: Year

Source: Calculated by the authors using Prowess data for the year 2012-13.

Relationship between CSR Expenditure and Profitability of Firms

There has been a lot of debate about the unnecessary burden on the corporate sector due to the CSR expenditure specified in the Companies Act, 2013. Corporate groups have criticised the mandatory clause in the Act, as it will decrease the profitability of firms. We have analysed the relationship between profit after tax and donation and community development expenditure undertaken by the firms over the last three years and find it to be positive and increasing.

Expenditure on CSR increases firms' profitability by building their image in the eyes of consumers, suppliers and the government. Firms also strategically differentiate their products from rivals' products in the market on the basis of CSR. CSR initiatives in local communities by environmentally polluting companies also help in avoiding protest movements and future governmental regulations. This reduces risks and uncertainties and increases the stability and returns of the firms. Therefore, CSR expenditure leads to higher profitability for all firm sizes as illustrated in Figure 5.

Figure 5: Correlation Between Profit after Tax and Socially Responsible Expenditure by Firms

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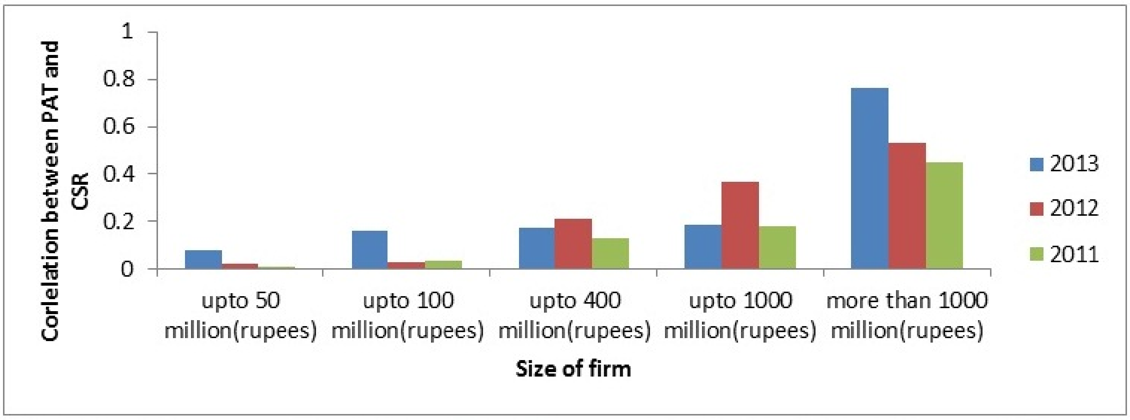

X-axis: Size of firms measured by Net Assets (in million rupees); Y-axis: Correlation between profit after tax and socially responsible expenditure by firms.

Source: Calculated by the authors using Prowess data for the year 2012-13.

We also find that that there is a positive correlation between CSR and profit, and the probability of higher spending on CSR increases as the firm becomes bigger. CSR as we know has evolved from philanthropy to community development to strategic CSR. Smaller firms with lesser resources at their disposal are less likely to adopt strategic CSR. They usually adopt philanthropy and community development activities such as schools for kids of employees, donations to religious organisations etc.

However, CSR activities closely linked to the company's business goals and falling in the purview of strategic CSR (for example–women hygiene classes by fast moving consumer goods majors) have higher payoffs and are mostly done by larger companies. Hence, positive correlation between profit and CSR expenditure is enhanced as the size of the firm increases. It is advantageous for a large company to spend on CSR, as it strategically differentiates its product, which ultimately pays off in the long run. Strategic differentiation may also spur innovation, which might improve delivery of services.

Pattern of CSR Expenditure by Major Firms in 2012-13

We studied the CSR activities undertaken by the top 200 firms by going through their annual reports for the year 2012-13 in order to better understand the nature of those activities and the driving forces that induced those activities. Although some studies (Singh and Aggarwal 2013) have looked at types of CSR activities undertaken by Indian companies, we have covered a larger number of firms across ten industries and have done an industry level analysis.

Until 2013, many firms had disclosed the activities undertaken by them, but not the exact amount they spent on each activity. We find that most of the firms undertake CSR expenditure for the welfare of rural communities, especially around their areas of operation. A possible reason could be to generate goodwill amongst people in the neighbourhood and

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become familiar with the area and its needs, which in turn would minimise costs of providing services. Contrary to the developed countries where CSR activities are undertaken mainly in the area of environment, in India it is mainly undertaken in the social sector.

In light of the recent legislation, it would be interesting to see how companies would change their CSR strategies. After community development, education (including skill development) attracts the largest share of CSR expenditure. Health is also a major area where firms like to invest. The following table gives an industry-wise breakup of the major CSR activities undertaken by each industry.

TABLE 1: Industry-wise Segregation of Major CSR Activities Undertaken by Firms in 2012-13.

Industry	Health	Education	Community Development/Rural Development	Environment	Total
Oil & Gas	23.50%	35.29%	29.41%	11.76%	100%
Automobile	40.00%	10.00%	40%	10%	100%
Consumer Durables	24.76%	21.34%	15.25%	28.75%	100%
Iron & Steel	35.29%	23.53%	35.29%	5.88%	100%
Banking & Financial Services	8.57%	20.00%	48.57%	35%	100%
Power	10.00%	10.00%	45%	35%	100%
Infrastructure	8.35%	30.55%	44.44%	16.66%	100%
Cement	22.20%	25.00%	29%	23.8%	100%
Paper &Pulp	19.90%	24.10%	18%	38%	100%
Pharmaceutical	30.00%	28.00%	22.00%	20.00%	100%

Source: Calculated by the author from the annual reports of the top 200 firms for the year 2012-13

Oil and Gas Sector: In the oil and gas sector, public sector undertakings have been found to spend the most on development of townships and community, with a special focus on education. They undertake community development in and around their areas of operation. This may be because the communities living close to their area of operation are most affected by negative production externalities. Hence the firms undertake CSR spending in order to reduce the negative effects of their production activities. They organise health camps, which provide free medical check-ups to people. For example, the Indian Oil Corporation runs mobile medical units in Mathura and has setup a nurse training institute in Digboi, Assam. It has also spent a lot on the school education of children who live near their plants and in their townships.

Iron and Steel Sector: In the iron and steel sector, the Steel Authority of India Limited (SAIL) has invested in health and education infrastructure for its employees. Many firms

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spend on skill development programmes, which help in building human capital leading to better employment prospects for people. The firms fund the school education of the children living in the nearby communities and give scholarships for higher education as well.

Banking Sector: Companies in the banking sector spend mainly on priority sector areas. They count the 40% mandatory priority sector lending as a part of their CSR activities. However, banks such as Jammu and Kashmir Bank undertake activities other than priority sector lending also. They support schools and provide funds for meeting educational expenses. Studies have shown that banks spend more on education and environment in order to strengthen their image and increase consumer satisfaction (Narwal 2007). Large banks tend to take on more CSR activities to signal better market performance, while relatively less profitable or smaller banks may want to increase their CSR initiatives to build stronger relationships with its stakeholders (Narwal 2007).

In a content analysis study, it has been found that Indian banks differ in their CSR orientation with respect to their ownership structure, number of employees, and date of its incorporation (Singh and Aggarwal 2011). It has been found that there is a significant difference in orientation in the areas of environment and rural development (when comparing banks with respect to ownership), in community welfare and environment and rural development (when comparing banks with respect to number of employees), and in environment and market place (when comparing banks with respect to the date of incorporation of the bank) (Singh and Aggarwal 2011). Indian banks no longer see CSR as charity, but they see it as a way of building their image and marketing their products.

Automobile Sector: Most of the companies in the automobile sector spend mostly on environmental sustainability, while some like Tata motors focus more on education and skill development. Mahindra and Mahindra focuses more on environment by committing to reduce greenhouse gas emissions. It has introduced various sustainability measures in its plants like xeriscaping, green buildings and water efficient plants. This can be attributed to the fact that the automobile sector is one of the most polluting industries in India.

The Centre for Science and Environment (CSE) has given a very low score to Tata motors and Mahindra and Mahindra in its green rating programme. Hence this may explain their CSR orientation towards environment. While Maruti Suzuki, which has a comparatively higher score in green rating, has spent more on employee welfare than on environment related activities. This suggests that firms which are comparatively more polluting are more driven towards environment in their CSR orientation. This may be to avoid possible future environmental regulations.

Cement Industry: Cement industry is one of the most polluting industries in India. Shree Cements which was given a very low rating by the CSE Green Rating programme has focussed more on sustainability. It has adopted the “triple bottom line” approach, where the focus is on profit maximisation, employee welfare and environmental sustainability. In its

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sustainability report, it has focussed on climate change and reduction of greenhouse gases during production.

Grasim Cements, which has a comparatively higher rating, has focussed more on community development and rural development. Their CSR spending has been directed towards health care, mother and child welfare and education. Gujarat Alkalies and Chemicals Limited (GACL) and Madras Cement Limited (MCL), which are subsidiaries of Ramco Cements, spend on community development and environment. GACL has undertaken clean development mechanism in order to reduce greenhouse gas emissions. Ultratech Cement's CSR strategy is oriented more towards community development. It has conducted health camps in rural areas around its plants and has encouraged sustainable livelihood through watershed management and environment.

Paper and Pulp Industry: In the paper and pulp industry, Ballarpur Industries (BILT) has focussed on sustainable development. Its CSR strategy focuses on rural development, with an emphasis on environment and communities. Similarly, JK Paper emphasises on social farm forestry and even publishes a bi-annual environment compliance report. Andhra Pradesh Paper Mills also focuses on environmental sustainability.

Power Sector: In the power sector, firms spend predominantly on community and rural development. They undertake development measures for communities which stay close to their plants through foundation and trusts. They emphasise on the provision of educational facilities and skill development programmes. For example, Jindal Steel carries out its CSR activities through its own trusts, which lead to saving of transaction costs and creation of goodwill in the local area. Public sector units like NHPC and NTPC focus on rehabilitation and resettlement of the communities displaced by construction projects. Since these plants cause damage to the surrounding areas, CSR activities may help in circumventing agitation by the local community and NGOs.

Consumer Durables: In the consumer durables and fast moving consumer goods industry, companies focus on healthcare and education. The Godrej group supports environmental sustainability by supporting conservation of mangrove forests and undertakes philanthropic activities in the health and education sector. They conduct blood donation camps, conduct cleft lip surgeries with Smile Train, a NGO. Similarly, *Hindustan Unilever* (HUL) focuses on improving health and well-being and reducing the environmental impact of its production activities. Hence in the consumer durable and fast moving consumer goods sector, we find that companies spend mainly on education and health initiatives.

Pharmaceutical Companies: Companies in the pharmaceutical sector spend mainly on education and health initiatives. Since pharmaceutical companies operate in the health sector and have enough skilled manpower, they conduct many health camps in rural areas. The thrust of their CSR activities is to make healthcare accessible to the marginalised sections of the society. Companies like Aurobindo Pharma, Cadila Healthcare, Sun Pharma

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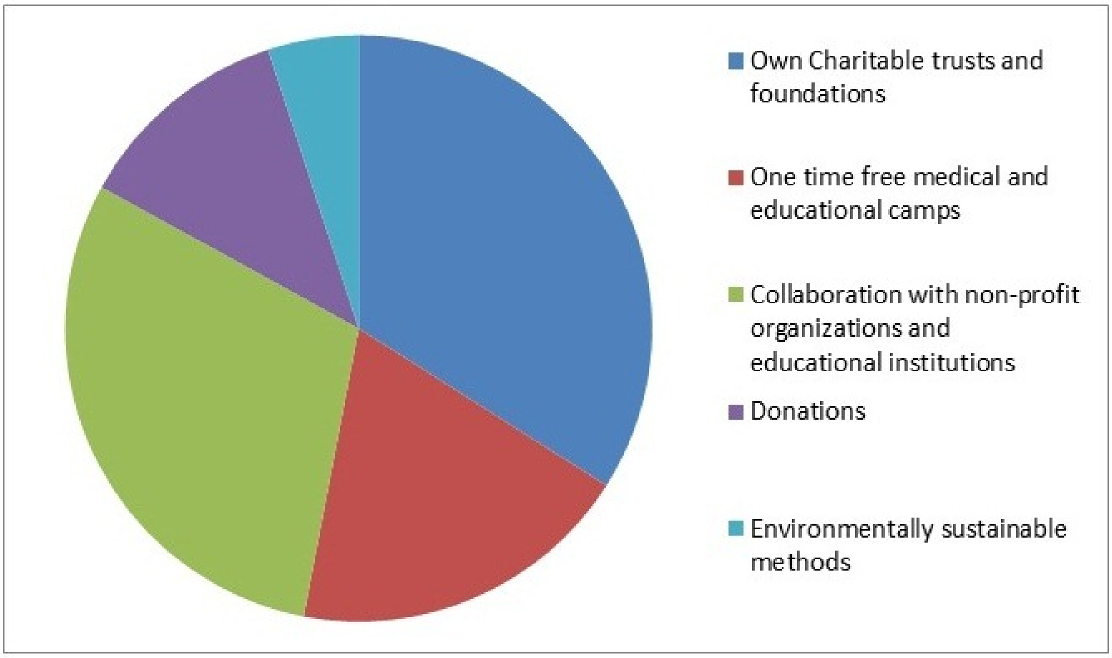
and Ajanta Pharma conduct medical camps, while GlaxoSmithKline focuses on the development of communities which reside near their plant.

Infrastructure Sector: In the infrastructure sector, firms spend heavily on community development programmes. We have taken firms engaged in construction, engineering, ports, shipping, road transport under infrastructure sector. These firms spend in the development of rural areas. They support the mid-day meal programmes in schools and skill development programmes for women and youth. When it comes to CSR implementation, we find that these firms undertake CSR mostly through foundations and NGOs.

Working Through their Own Foundations and Trusts

The following pie chart depicts the various approaches adopted by the top 300 firms to fulfil their CSR obligations.

Figure 6: CSR Implementation Approaches Adopted by the Top 300 Firms



Source: Calculated by the author using data from the 2012-13 annual reports of companies.

We found that 34% of the top 300 firms in India work through own foundations or trusts. They serve the society through various measures like community development, rural development, etc. About 19% of the companies organise free medical check-up camps in rural areas, blood donation camps and educational camps for farmers in the rural areas and school children. Around 30% of the firms collaborate with non-profit organisations to carry out their CSR activities. For example, some companies like TVS motors, Godrej and other companies fund the NGO Smile Train, which conducts cleft lip and palate surgeries.

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Tata Motors collaborates with a number of industrial training institutes to conduct skill development programmes. Some of the companies collaborate with government schools and support the mid-day meal programmes. Around 5% of the companies adopt environmentally sustainable methods of production. These firms belong mostly to the environmentally polluting industries like paper and pulp. Most of the firms in the paper and pulp industry come out with a bi-annual environmental report on environmental compliance as directed by the Ministry of Environment and Forest. 12% of the firms make donations to local schools and hospitals. Mostly banks donate medical equipment and school books to local hospitals and schools.

Hence, it can be seen that most of the firms rely on foundations to carry out CSR activities. In this way they are able to monitor the CSR activities better, save on transaction costs and create goodwill for their company.

Concluding Remarks

The concept of CSR has the potential to bring a revolution in the development of the economy. With rising fiscal deficit and leakages in the welfare schemes, CSR seeks to address the problems of society in a cost effective manner. The concept has the potential to generate Rs 20,000-25,000 crore[1] every year, which can give a boost to investment in human and physical capital. Presently, CSR expenditure is mostly incurred at the local level through the foundations established by firms. This aligns CSR initiatives with the ideology of the firm and minimises transaction costs for it. For efficient utilisation of funds allocated for CSR and full realisation of potential benefits, these expenditures need a direction.

The recent commitment of Rs 100 crore each, by two leading companies, Tata Consultancy services and Bharti Airtel, as a part of their CSR initiatives to build toilets for girls in schools in the wake of government's Swachha Bharat Abhiyan is only the tip of the ice-berg. Some more thought needs to be given to the most pressing problems of society and whether CSR resources could be utilised to address them. Contrary to some pessimistic voices in the society, CSR expenditure may not affect profits adversely and could help in building the brand name of the firm.

Though the new Companies Act, 2013, which made spending 2% of their profits on CSR mandatory, came into force only in April 2014, the last couple of years have seen a significant increase in CSR expenditure by firms. This can be attributed to the desire of companies to project themselves as socially responsible. The CSR expenditure by firms is affected by the industry to which they belong. Firms in polluting industries spend more on activities related to the environment, while firms in the iron and steel and power sector spend more on local community development, as their projects cause large-scale displacement. They also do it in the hope that it might prevent future boycott and protest movements.

Until now, donations by firms were driven by their interests; it was arbitrary, and in some

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cases very small in comparison to the size of the firms. The CSR activities of the firms depended upon the nature of their industry and restricted to the area where the firm was located. This was largely driven by factors such as cost minimisation and “visibility” among the consumers. But this may change with the new law. Firms may be driven to diversify their areas of operation and part of population which had been left behind in the development process may gain tremendously from this.

Notes

[1] Approximate value calculated by aggregating 2% of the profit-after-tax across all eligible companies.

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