Thomas Schmidheiny Centre for Family Enterprise

Family Businesses: Heeding the Call of Corporate Conscience 2015-2017

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Abbreviations

CBDT	Central Board of Direct Taxes
CPSE	Central Public Sector Enterprise
CSPM	Centralized Scrutiny and Prosecution Mechanism
CSR	Corporate Social Responsibility
DPE	Department of Public Enterprises
EC	European Commission
FBGF	Family Business Group Firm
FY	Financial Year
GOI	Government of India
HLC	High Level Committee
I-T Act	Income Tax Act of 1961
MCA	Ministry of Corporate Affairs
MNC	Multinational Company
NF	Standalone Non-Family Firm
OBGF	Other Business Group Firm
ROC	Registrar of Companies
SEBI	Securities and Exchange Board of India
SFF	Standalone Family Firm
SOE	State-Owned Enterprise

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Executive Summary

In the last few decades, Corporate Social Responsibility (CSR) has become an integral part of the public discourse with academicians, practitioners, policy-makers and media laying stress on equitable outcomes through business-society interactions. While there was a general agreement that businesses needed to do more to be socially and environmentally responsible, a far-ranging debate has ensued amongst various stakeholders to determine the exact nature of these obligations. In this backdrop, the Government of India passed a prescriptive law under the Companies Act of 2013 making CSR mandatory for certain class of companies from the financial year (FY) 2014-15.

Studying the CSR spends of companies in India remained limited to certain large firms who had a well-documented history of philanthropic initiatives. With the advent of the CSR law, firms now must make mandatory disclosures of social spends as per a standard prescribed format. This has provided a unique opportunity to study the characteristic differences in the CSR spend behaviors of family firms and non-family firms across a large set of representative firms given the uniform regulatory landscape. Recent research with respect to CSR has been undertaken in the developed countries context whereas systematic studies in the emerging economies context, where different socio-economic, institutional, legal and corporate landscapes prevail, remain sparse.

Therefore, the Thomas Schmidheiny Centre for Family Enterprise at the Indian School of Business has conducted this study, for the three-year period between FY 2015-2017, to understand heterogeneity in behaviors across different categories of firms based on ownership structures. Apart from the quantum of spends, we have looked at the nature of spends covering the areas of development selected by the different categories of firms while also throwing light on the implementation modes chosen to spend their CSR monies.

Our results show that Family Firms have a greater pre-disposition to meet the CSR compliance under the law and we find that the historical context and theoretical frameworks are aligned with these findings. In wanting to create lasting organizations, family firms institutionalize enduring values that reflect in the engagement in social welfare activities across generations. However, family firms undertake these activities directly either through in-house teams or company-owned foundations which are also known to be controlled by family members. It leads to the argument that this would expropriate any benefits for minority shareholders in building a positive legacy for the family. Therefore, it is argued that family-owned firms professionalize their social pursuits and build transparent and strong governance mechanisms in the interest of their firms.

With respect to the CSR policy – it remains a work-in-progress given that India was the first country to develop such a prescriptive law. Several gaps emerge through our study which need to be addressed by policy-makers to create enough incentive other than the statutory provisions for firms given that more than 50 per cent of all firms in our sample remain non-compliant. Simultaneously, firms would do well to understand a well-defined CSR strategy has several advantages in the long-term. Without enlightened promoters aided by independent directors and a complementary policy framework – universal adoption of well-meaning and highly spirited CSR pursuits will continue to remain a distant dream.

1. Introduction

Family firms have played a significant role in employment generation and wealth creation in the Indian context. As a result, they have not only contributed to the national exchequer through direct and indirect taxes but have also over the years, of their own volition, taken part in social welfare activities[1]. In the past two decades, the social obligations of firms across the world have gradually moved towards greater formalization and regulation by national and intergovernmental organizations. This has been necessitated by the rising income inequality and other social and ecological imbalances that have manifested itself with the globalization of the economy.

The imbalance has become even more evident in India, where businesses prospered post liberalization and created wealth for promoters and other shareholders, but 21 percent of the population still lives in extreme poverty[2] and the country is home to 50 percent of the world's malnourished children[3]. Consequently, the role of the corporation in the narrative of creating socially equitable outcomes has become inevitable in the light of this glaring divide between the haves and have-nots.

Over the years, scholars and practitioners have conceptualized the firm's social obligations in different terms such as: corporate philanthropy; corporate sustainability; corporate citizenship; economic, environmental and social imperatives of the triple-bottom line approach; and environmental, social, and governance (ESG) investment parameters. The term "Corporate Social Responsibility" (CSR) has come to encompass the broad and varying perspectives of business-society interactions preceding it[4]. Nidumolu and Kallapur (2015) find that even though the roots of CSR are found to be in philanthropy, the concept of CSR when viewed from the lens of sustainability – that instead focuses on the development of far-sighted and responsible business practices with an eye towards future social and environmental challenges and, in turn, have long-term economic concerns – introduces a strategic business concept that is not evident solely from its philanthropic angle.

The 'Business Case' for CSR

It would be a misconception to believe that CSR has an exclusive non-business objective. Carroll (1979) in his seminal work on three dimensional CSR activities argued that it was not possible to separate social responsibilities of a company from its economic, legal or ethical responsibilities; and hence, its degree of social responsiveness would have economic considerations. Porter & Kramer (2006) posit that betterment of society and long-term corporate performance are not at odds but are rather interdependent. In creating shared value, companies could uplift a society

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[1]PwC India Family Business Survey 2016 -https://www.pwc.in/assets/pdfs/publications/family-business-survey-2016/pwc-india-family-business-survey-2016-aligning-with-indias-growth-story.pdf

[2]Extreme Poverty - Living on US$1.90 per day; Source:World Bank Country Poverty Brief - October 2017 http://databank.worldbank.org/data/download/poverty/33EF03BB-9722-4AE2-ABC7-AA2972D68AFE/Archives-2017/Global_POV_SP_CPB_IND.pdf

[3] India has the largest number of undernourished children in the world - https://www.livemint.com/Politics/OIdNvn30nqdrGQC6pARu3J/India-has-largest-number-of-malnourished-children-in-the-wor.html

[4]United Nations Industrial Development Organization (UNIDO) - What is CSR? https://www.unido.org/our-focus/advancing-economic-competitiveness/competitive-trade-capacities-and-corporate-responsibility/corporate-social-responsibility-market-integration/what-csr

from which it employs an educated and healthy workforce while the efficient use of natural resources would make it more productive.

Other researchers claim that a well-defined CSR strategy helps the firm maintain its social license to operate within communities (Steger, 2006; Schaltegger & Burritt, 2010), attract and retain talent (Bhattacharya et al, 2008; Meister, 2012), enhance corporate reputation (Fombrun, 2005; Ramachandran, 2015) and lead to improved access to capital by attracting foreign institutional investment (Oh et al., 2011; Panicker, 2017), amongst other benefits. As per a Deutsche Bank study by Fulton et al. (2012), firms evaluated positively on ESG parameters have a lower cost of capital and provide greater returns than the market in the mid to long term investment horizons.

Further, researchers such as Elliott et al. (2014) find that a positive CSR performance, that is performance that rates highly on factors such as philanthropy, employee safety, greenhouse emissions and workforce diversity, leads to higher estimates of fundamental value of the company, specifically by investors who do not explicitly assess the CSR performance. In employing a resource-based view, Branco & Rodrigues (2006) and McWilliams & Siegel (2011) provide that, when CSR can achieve the above-mentioned benefits, it leads to strategic competitive advantages and, as a result, create long-term value for shareholders (Godfrey et al., 2009).

Despite this rising awareness and strategic distinction of CSR widespread adoption of voluntary CSR continued to be muted in India (Bird et al., 2017). Consequently, the Government of India (GOI) passed the mandatory CSR law under Section 135 of the Companies Act of 2013 which required a certain class of companies to spend at least 2% of the average net profit towards CSR activities and make mandatory disclosures about their spending. Prior to the implementation of the Act, reporting and disclosures of voluntary CSR spends were not widespread or consistent (Panicker, 2017). Therefore, a systematic large-sample study of the CSR behaviors of family firms vis-a-vis non-family firms was not possible in India.

It is in this context that the Thomas Schmidheiny Centre for Family Enterprise at the Indian School of Business has undertaken an explorative study to examine the systematic differences in the CSR behaviors of different categories of firms in the first three financial years of the implementation of the mandatory law i.e. 2014-15, 2015-16 and 2016-17. Statutory reporting disclosures related to a wide range of parameters that include CSR spends, development sectors targeted for intervention and the mode of implementation have been made available for these certain class of listed companies in their annual reports. Our first study, "Family Businesses: The Emerging Landscape"[5], divided 4,809 listed firms into family firms and non-firms[6]. Further, these were divided into subgroups defined by their affiliation to business groups and other ownership categories such as state-owned enterprises and multinational companies[7]. Consequently, we were able to build a final subsample of 1210 unique listed companies that fall in the purview of the CSR law.

We find that a greater proportion of family firms meet and go beyond the 2% CSR spend as compared to non-family firms. Delving deeper, we find that state-owned enterprises (SOEs) are

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[5] Family Businesses: The emerging landscape - 1990-2015: http://www.isb.edu/sites/default/files/WP-FB-The-Emerging-Landscape_0_0.pdf

[6] For a detailed description of identification of family firms see Appendix 1

[7] For a detailed description of SOEs, BGs and MNCs see Chakrabarti & Ray (2016) and Appendix 2

driving CSR initiatives along with family business group firms (FBGFs). Standalone family firms (SFFs) and multinational companies (MNCs) follow suit and are not too far behind in terms of their average CSR spends. Widely-held non-family firms in our sample - standalone non-family firms (NFs) and other business group firms (OBGFs) - are significantly lagging behind the other firms. Additionally, we find that unintended tax benefits have skewed spending to a limited set of areas reflecting expediency in the approach to CSR across the board. We also find that family firms prefer direct routes of implementing CSR monies either through the company-owned foundations in case of FBGFs or in-house CSR department in case of SFFs.

The rest of study explores the antecedents and possible reasons for the heterogeneity in normative CSR behaviors of the firms in the sample. The paper is structured in the following manner: Section 2 discusses the background of CSR in India - including its evolution with respect to different ownership structures and the role of the GOI in shaping legislative action around CSR; Section 3 describes the data and methodology to select our cohort of firms for analysis; Section 4 throws light on the consolidated performance of categories of firms in our cohort over a three-year period with year-wise snapshots; Section 5 elucidates the nature of spend vis-a-vis the development sectors and areas targeted; Section 6 explores the mode of implementation adopted by our cohort of firms; Section 7 provides conclusions and implications of the study while discussing the effectiveness and the implications of the CSR policy and the way ahead.

2. Background

Corporate social responsibility in India has been guided and shaped by distinct periods in its socio-economic, cultural and political evolution. These forces have had a marked effect on the social behaviors of different categories of firms in the Indian landscape and was first observed in an organized manner in pre-independent India. The antecedents of CSR provide insights in the motivation of different categories of firms to undertake such activities.

CSR and it's Evolution in India

Kumar et al. (2001) recognize four models of corporate responsibility that have in some form or other been practiced in India over the years. These include the Ethical, Statist, Liberal and Stakeholder approaches to CSR.

1. Ethical CSR

In early to middle twentieth-century India, the idea of Ethical CSR took shape in the Gandhian doctrine of trusteeship. Corporate philanthropy came into existence, which evolved from the earlier charitable endeavors that were driven by religious and cultural traditions of the individual promoters and their families (Sundar, 2013; Ramachandran, 2015; Chakrabarty, 2015). This approach emphasized that businesses were trustees of society's wealth and were, hence, responsible for conducting activities that were in the interest of public welfare.

Family groups such as Tata, Birla, Bajaj and Godrej amongst others were the first to respond to this ideal and established their philanthropic foundations. These business houses played a prominent role, first, in the freedom struggle and then in nation building post-independence, with the establishment of key institutions in education, research and healthcare (Lala, 2004; Sundar, 2013; Chakrabarty, 2015). The philanthropic traditions amongst many Indian business houses today towards external stakeholders, particularly family businesses, can be attributed to these developments in the pre-independence era (Sharma, 2009; Sundar, 2013).

2. Statist CSR

Post-independent India embraced Soviet-style highly centralized economic policies and planning that were championed by the first Prime Minister Jawaharlal Nehru in a bid to achieve self-sufficiency (Sanders, 1977). The introduction of high tariff duties and taxation on the private sector along with curbs on imports and private and foreign investment led to the dominance of SOEs whose key mandate was social welfare (Kaushik, 1997). The Statist CSR approach was conceived and implemented by these SOEs, especially in the sphere of community and employee welfare in the period between 1947-1990. The essence of the state-led corporate responsibility is still observable in the many SOEs that operate even today (Kumar et al., 2001)

3. Liberal CSR

In the early 1990s, India reformed its economy in the face of chronic balance of payment deficits. This period witnessed the privatization and deregulation of the economy to promote private and foreign investments. India opened itself to the global economy and experienced a period of rapid economic growth with the spurt of foreign and private investments in the country (Kaushik, 1997). Much of the corporate thinking and management literature in the developed countries was aligned with Friedman (1970), espousing a liberal perspective of CSR which emphasized the firm's sole objective to provide economic value to its immediate stakeholders within the ambit of the law (Kumar et al., 2001). Given the worldwide trend of increasing privatization and deregulation, a few Indian businesses may have been influenced by this thought process, however, on the contrary, the general willingness of businesses to giving increased with rising profits amidst a surge of public and government expectations of business (Sharma, 2009).

4. Stakeholder CSR

However, at the turn of the century, a decade after globalization, the thinking towards social responsibility grew to accommodate wider sustainability concerns considering the "imbalance between the economic, social and political realms" as pointed out in 1999 by then United Nations (UN) Secretary General Kofi Annan[8]. In 2003, ninety large Indian corporates became part of the Global Compact[9,10], the UN's corporate citizen initiative, which outlined the greater need for multi-stakeholder approach to meet its social obligations (Kell, 2003). The global view had now shifted to adopt Freeman's (1984) stakeholder approach to managing business-society interactions and both – the MNCs who brought this thought process to India and the Indian firms with global aspirations and business networks – imbibed it into their CSR strategies in the wake of rising civil society activism and media spotlight (Balasubramanian et al., 2005; Freeman et al., 2007; Sharma, 2009; Sundar, 2013). However, CSR remained limited to "a collection of good citizenship/philanthropic activities undertaken by only the largest business houses" as per Afsharipour (2011).

Role of the Government

The GOI had played only a passive role since independence in 1947 with respect to CSR. It defined certain suggestive directions for companies that chose to undertake CSR until 2009 (Gatti et al., 2018). In the period between 2009-2012, however, the policy intent of the GOI shifted towards proactive encouragement of corporate involvement in adopting their social responsibilities (Figure 1).

The Guidelines on CSR and Sustainability for Central Public-Sector Enterprises (CPSE) drafted by the Indian Department of Public Enterprises (DPE) in 2010 first signaled the GOI's intent towards mandatory CSR with central government owned SOEs required to institute and stipulate CSR spends in their annual MoUs with the DPE (Subramaniam et al., 2017). Realizing that voluntary framework of CSR had not evoked the desired response for other companies, the GOI decided to pursue a uniform mandatory CSR law approach with the Companies Act of 2013.

India had, thus, become the first country to mandate a defined CSR spend and only one of three countries, along with Indonesia (Waagstein, 2011) and Philippines[11], to undertake legislative action to mandate CSR.

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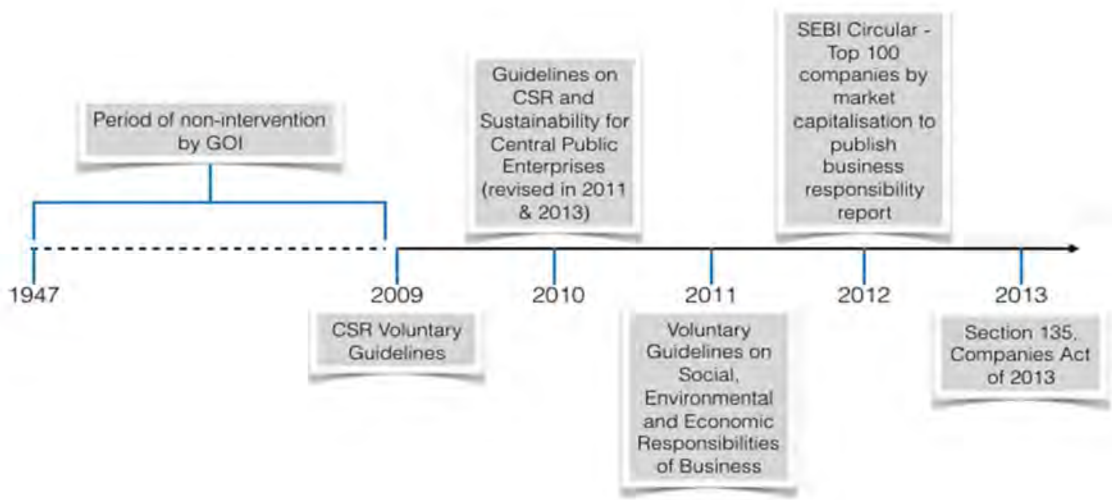
[8] https://www.un.org/press/en/1999/19990201.sgsm6881.html

[9] http://globalcompact.in/

[10] https://www.unglobalcompact.org/what-is-gc/mission/principles

[11] http://www.congress.gov.ph/legisdocs/basic_17/HB02161.pdf

Figure 1: Timeline of CSR Regulations



Section 135 of the Companies Act of 2013

As per Section 135 of the Act of 2013[12], any company[13] registered in India and having either

(1) a net worth of INR 500 crore (INR 5,000 million) or more
(2) a turnover of INR 1000 crore (INR 10,000 million) or more
(3) a net profit of INR 5 crore (INR 50 million) or more, in any financial year,

was now required to spend 2% of their average net profits[14] of the immediately preceding three financial years with a preference given to local areas in which the company operates.

Further, the mandatory law laid out a clear role for board of directors of any such company (Figure 2). The board had to constitute a CSR Committee comprising at least three directors, one of whom was required to be an independent director, to recommend and monitor CSR activities. To ensure compliance, companies were required to provide for an annual report on CSR activities in the annexure of the Board's Report in a format prescribed by the Ministry of Corporate Affairs (MCA)[15,16]

Firms that cannot meet the 2% prescribed limit are only required to provide the reasons for not spending the amount.[17] Further, the firms are free to decide if they want to carry forward the unspent amount to the next financial year.[18] Penalties occur only if a company fails to conform to

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[12] Section 135 of Companies Act, 2013: http://www.mca.gov.in/SearchableActs/Section135.htm

[13] Being a holding or subsidiary company of a company, which fulfils the criteria under section 135(1), does not make the company liable to comply with section 135, unless the company itself fulfills the criteria

[14] Calculated as per Section 198 of the Companies Act, 2013: http://www.mca.gov.in/SearchableActs/Section198.htm

[15] MCA Notification, 27th Feb 2014: http://www.mca.gov.in/Ministry/pdf/CompaniesActNotification2_2014.pdf

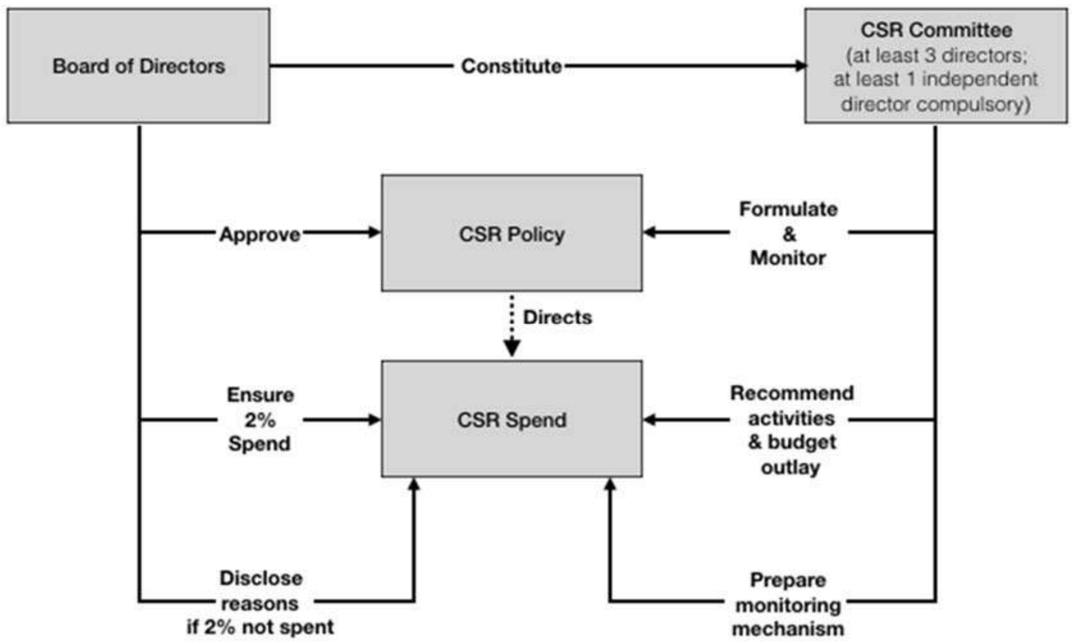
[16] As per Rule (3) of Section 135 states that a company ceases to have any obligation if it remains ineligible for a period of 3 consecutive years till the company again meets the criteria

[17] Clause 8 of Section 134, Companies Act, 2013: http://www.mca.gov.in/SearchableActs/Section134.htm

[18] http://pib.nic.in/newsite/PrintRelease.aspx?relid=137505

the stipulation that requires that the company state reasons for not spending the mandatory 2% in its report of CSR activities as per Section 134 of the Act of 2013[19]. Companies not reporting or disclosing information were punishable by fines from INR 50,000 to INR 25 lakhs (INR 2.5 million) with defaulting officers punishable with a jail-term which may extend to three years or a fine from INR 50,000 to INR 5 lakhs (INR 500,000) or both.

Figure 2: Role of the Board



Researchers Cominetti & Seele (2016) defined a framework to evaluate CSR regulations, which deconstructed stipulations as either hard or soft. Hard laws were those that carried mandatory legal requirements for companies while soft laws were those that advocated voluntary uptake of CSR implying self-regulatory mechanisms. However, considering multiple guidelines, standards and laws, the classification cannot be strictly binary as the degree of obligations and sanctions defined vary considerably and could be, instead, viewed in the continuous space of the two-dimensional matrix (Figure 3).

Given the "comply or explain" stance of the GOI, it is plausible that the Section 135 of Companies Act, 2013, can be interpreted as a "soft hard" law. Further evidence for the same is found in the report of the high-level committee constituted by MCA in 2015. The Baijal Committee recommended that leniency be shown to non-compliant companies in the first "two or three years" after the enactment of the mandatory CSR law. Additionally, they felt that the "comply or explain" stipulation of the law should be sufficient disincentive against non-compliance putting the impetus on boards of the companies to regulate themselves in full glare of the public.[20]

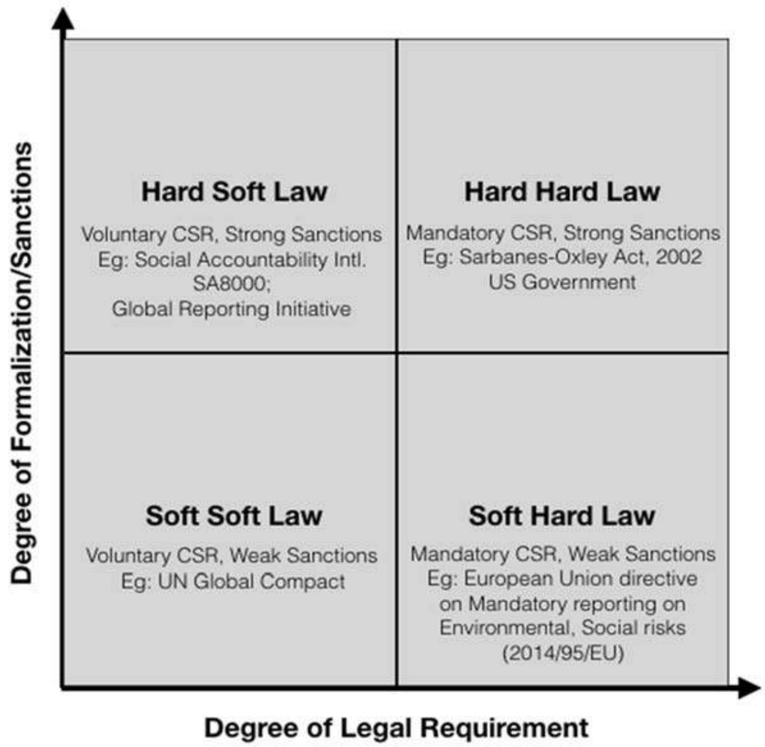
The lack of institutional monitoring mechanism by the GOI implies that companies' CSR behaviors would not be driven by fear of sanctions but to a large extent by the conscious volition of the

[19] Clause 8 of Section 134: http://www.mca.gov.in/SearchableActs/Section134.htm

[20] http://www.mca.gov.in/Ministry/pdf/HLC_report_05102015.pdf

company's directors in our period of study i.e. financial years 2014-15, 2015-16 and 2016-17. Board representation is strongly linked to ownership structures and patterns as directors are representatives of the shareholders. Therefore, we predict that the categories of firms in our classification will exhibit heterogeneity in their CSR trends not influenced entirely by the legal mandate.

Figure 3: Different CSR Regulatory Forms (Cominetti and Seele, 2016)



3. Data and its Description

Section 135 of the Act of 2013 mandates eligible companies provide an annual report on CSR activities in the prescribed format as defined by the MCA[21]. For listed companies, this report must be furnished as an annexure to the director's report in the Annual Report which is publicly available. This disclosure is required to be vetted by the Chief Executive Officer or the Managing Director along with the Chairman of the CSR Committee and duly incorporated in the Form called AOC-4 in the yearly e-filing with the MCA.

The number of meetings in the financial year of all board level committees which include the CSR committee are also to be disclosed in the report on corporate governance under the statutory disclosures for board-level committees. The data provided in the disclosures provide for rich analysis, however, extracting this information for a large sample of companies from their annual reports would be time consuming and tedious.

With the GOI initiating the Government "National CSR Data Portal" (CSR portal)[22,23]in January 2018 and company specific data being made available to the public, we could readily extract the data albeit for only a few of the items specified in the disclosure which can be divided into firm-year variables and project-level variables (Figure 4).

Figure 4: Firm-Year Variables and Project-level variables

The study was limited to a specific set of companies listed on the BSE and NSE, which we had classified into family firms and non-family firms as per earlier work completed by us at the Thomas Schmidheiny Centre for Family Enterprise. The Centre has classified firms into family firms and

[21] For detailed prescribed format as defined by MCA see Appendix 3

[22] http://pib.nic.in/newsite/PrintRelease.aspx?relid=175763

[23] https://csr.gov.in/CSR/

non-family firms on the basis of minimum ownership of 20% equity shares by the family members and management control or succession/business continuity.[24]

The family firms are further classified by the Centre into Family Business Group Firms (FBGF) and Standalone Family Firms (SFF) and the non-family firms into State-owned enterprises (SOEs), Multinational subsidiaries (MNCs), Other Business group affiliated firms (OBGFs) and Standalone non-family firms (NFs)[25].

In ensuring that no wide-ranging errors existed in the data at least with respect to firm-year variables, we ran a series of intra-variable and inter-variable checks to check for glaring errors. Further, data from Prowess DX database of CMIE, which makes available firm-year variables for CSR, was incorporated and large variances were manually checked against the annual reports of the companies. In the interest of reporting the larger trends at an aggregated level, we have taken the data as it is for the project-level variables from the Government CSR portal with only the data of a few companies, chosen on an adhoc, basis verified at a granular level. It is also worthwhile to mention that the open-ended nature of the prescribed format has led to non-standardized reporting of CSR activities especially of project-level variables with glaring omissions and obfuscations by companies.[26]

Data was extracted for nearly 2,145 listed companies. Firms which had no fill rates or were eligible under the CSR clause only for a single year out of the three possible financial years were culled from the sample. This left us with 1,389 listed firms. Additionally, as we were looking to make comparisons in behavior and considering the lack of clarity that existed in the initial years, we have limited our sample to firms that became eligible in the financial year 2014-15 to ensure equal footing. Therefore, a total 1,210 firms were eligible in the sample finalized for our analysis which corresponds to 3,630 firm-year observations and 16,470 project-level observations.

Family firms comprise 87% of our sample of which SFFs were 46% of the family firms (Figure 5). The reduction in the number of SFFs as compared to our previous two studies in this series could be attributed to the fact that a large number would not have qualified under the eligibility clause for mandatory CSR. The number of MNCs and SOEs in our sample comprised majority of the non-family firms in accordance with the past two studies. NFs and OBGFs formed nearly 2.3% of our sample of firms (Table 1).

Considering the variability that may exist in the CSR spends over the years, we have aggregated the CSR prescribed expenditure over the period of three years and we study the concomitant spends made by firms to get a holistic understanding of their behaviors in this period.

[24] For a detailed description of identification of family firms see Appendix 1

[25] For a detailed description of SOEs, BGs and MNCs see Chakrabarti & Ray (2016) and Appendix 2.

[26] https://www.livemint.com/Opinion/h9kceM8LpU9nHNJ5xqyCVL/How-CSR-is-reported-is-critical-too.html

Figure 5: Distribution of Firms in the Sample

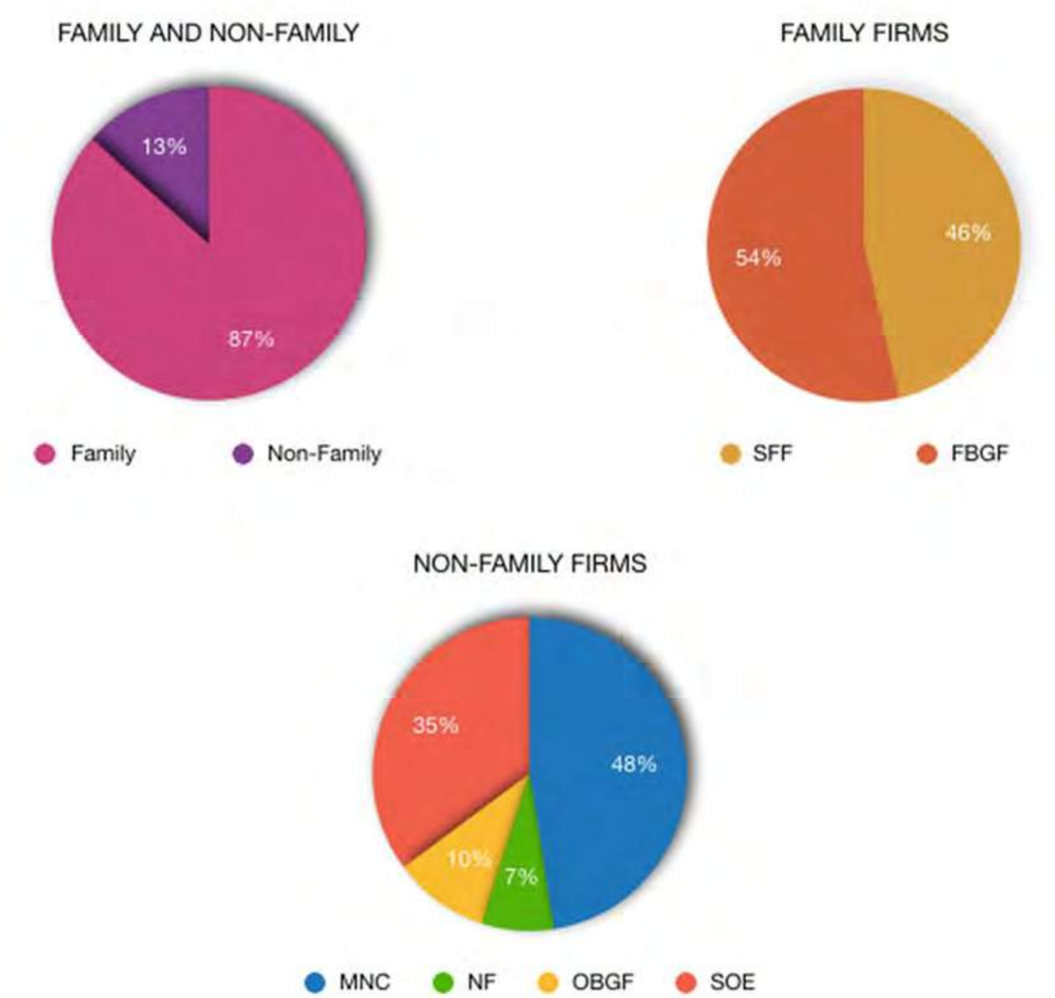


Table 1: Distribution of Firms in the Sample

Ownership Categories	Number of Firms
Family Business Group Firms (FBGF)	562
Standalone Family Firm (SFF)	486
Multinational Companies (MNC)	77
State Owned Enterprises (SOE)	57
Non-Family Standalone Firm (NF)	12
Other Business Group Firms (OBGF)	16
Grand Total	**1210**

4. CSR Performance

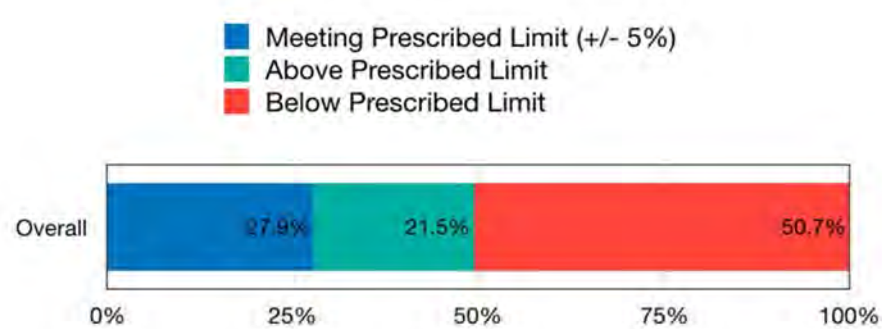
In our previous study: "Family Businesses: Promoters' Skin in the Game- 2001-2017"[27], we had explored the ownership patterns of listed firms in India. The study revealed that ownership has implications for strategic priorities (Daily & Thompson, 1994) and decision-making processes of the firm (Kaur & Gill, 2009). It follows that CSR performance of the firms could be driven by ownership structures.

Research attributing CSR performance to ownership structures remains sparse with relatively little light thrown on the behaviors in the emerging economy context. Oh et al. (2011) in the Korean context and Panicker (2017) in the Indian context have worked on how ownership characteristics affect CSR behaviors based on the percentage of shareholding across different promoter and non-promoter groups. In contrast, our study aims to derive insights about CSR behaviors across well-defined mutually exclusive categories of firms based on not only degree of shareholding but control of the company through board and senior management positions. Further, these firms have been systematically divided by our Centre into representative subclassifications to obtain a more granular understanding of CSR performance.

Rampant Non-Compliance of CSR Law

Before we explore the systematic differences in CSR performance in ownership structures, a key trend must be pointed out with respect to all firms in our sample. More than 50 percent of firms in our sample are non-compliant with the CSR law over a three-year period (Figure 6a). It brings into question, first, whether the policy has managed to create enough incentives for businesses to take up CSR. Second, given the lack of monitoring mechanism, the companies were given considerable leeway through the "comply or explain" approach, – it has to be asked if this approach worked.

Figure 6a: Proportion of Firms Meeting Prescribed CSR Norms



As far as the first question is concerned, even though the policy mandates CSR, it is imperative for promoters/managers to consider its advantages as extant literature points out. Those companies that have incurred sustained losses and are facing weak cash positions do have rightful grounds to not meet their social obligations in lieu of meeting urgent business expenses to ensure survival. However, a good portion of companies have not provided reasons in their

[27] "Family Businesses: Promoter's Skin in the Game": https://www.isb.edu/sites/default/files/Family_Business_Promoters_skin_in_the_game_1.pdf

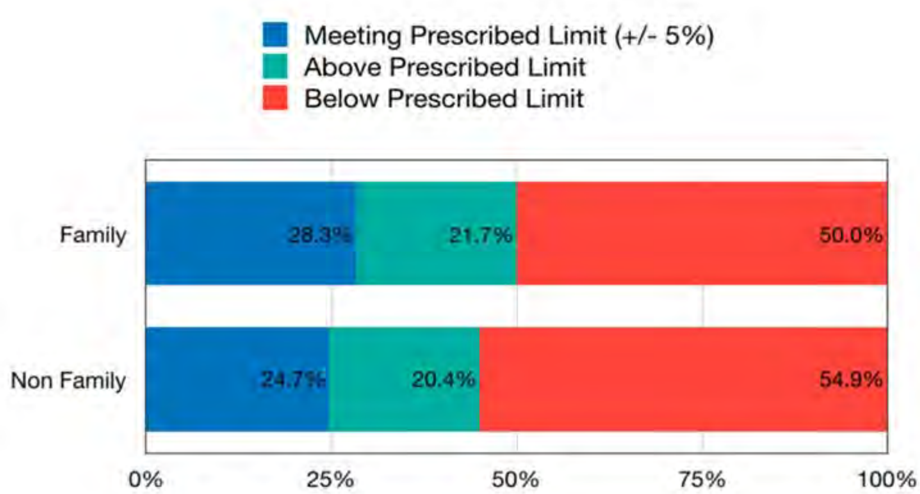
board reports while industry experts have been skeptical about the validity of other reasons provided such as "long term nature of social projects" or "unable to identify implementing agencies or projects"[28,29], which shows a lack of intent in the adoption of CSR practices. Policymakers will have to determine how policy can create necessary and sufficient incentives for greater adoption of CSR.

With respect to second question, Robichau & Lynn (2009) find that for successful implementation of any policy, the supporting administrative, monitoring and governance mechanisms should be given utmost importance. Given the non-compliance in the first three years, the MCA has created a Central Scrutiny and Prosecution Mechanism (CSPM) to review CSR spending of companies retrospectively. As of August 2018, reports[30] suggest that 272 companies are facing violations for non-compliance in the financial year 2015-16, hinting that the grace period has ended for companies under the law as GOI has now moved to a stance of 'comply or get prosecuted'. This indicates a shift towards a hard-hard law approach by the GOI. Whether this approach is necessarily going to drive long-term quality CSR programs, only time will tell.

Family Firms vs Non-Family Firms

A greater proportion of family firms in our sample have met their mandated CSR obligations as compared to non-family firms (Figure 6b). Building on the behavioral agency model, Gómez-Mejía et al. (2007) found that the primary reference point for family firms is the loss of socioemotional wealth, it can be argued that family firms are concerned with non-economic utilities.

Figure 6b: Proportion of Firms Meeting Prescribed CSR Norms



Therefore, family firms would value a strong need for self-identification (Kepner, 1983; Gómez-Mejía et al., 2007); acts that enhance their corporate reputation (Deephouse & Jaskiewicz, 2013); and activities that result in increased social status in the community (Miller & Le Bretton-Miller,

[28]https://www.thehindubusinessline.com/opinion/csr-has-to-be-made-more-meaningful/article21696489.ece1

[29]https://www.thehindubusinessline.com/companies/csr-spending-16-of-firms-give-no-reason-for-not-meeting-obligations/article8871605.ece

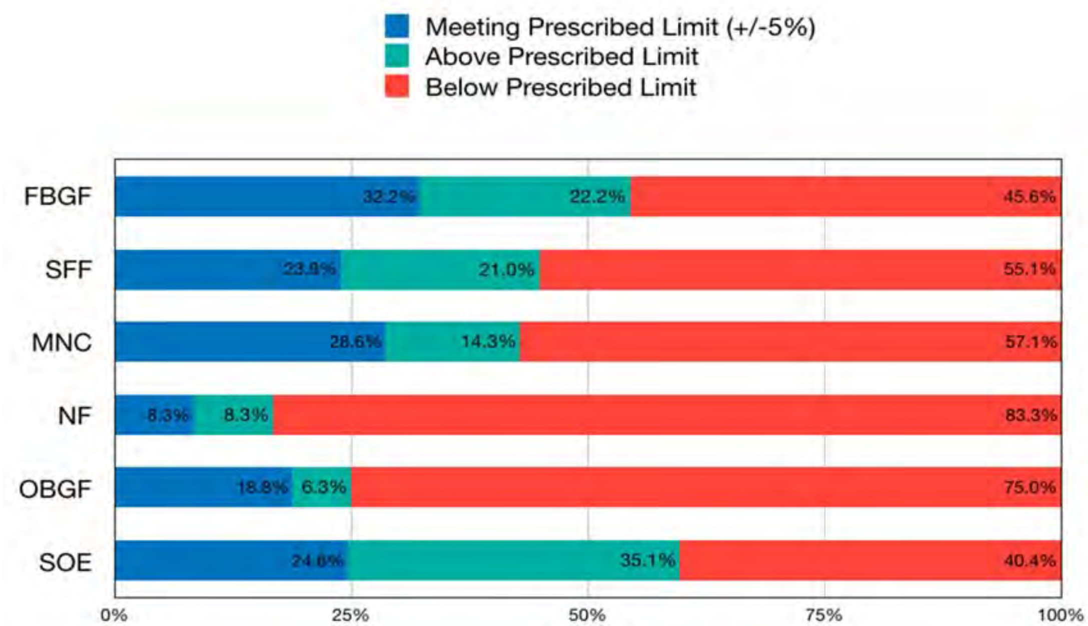
[30]https://www.livemint.com/Companies/Va2pXNjp4UB0Kggez0HPMK/Corporate-affairs-ministry-issues-notices-to-272-firms-for-n.html

2014). To gain socioemotional rewards, Berrone et al. (2010) find that family firms are more responsive to the institutional pressures of local communities. They do so in a meaningful manner in comparison to non-family firms, keeping in mind the impetus on social legitimacy independent of any economic concerns. Cennamo et al. (2012) suggest that family firms are known to undertake “proactive stakeholder engagement” activities to further their socioemotional wealth. A PwC global survey[31] (including India) of family business leaders even found that 71 percent of 2,802 respondents considered contributing to society and the community and leaving a positive legacy behind as the fourth most important business and personal objective.

Business Group Affiliated Firms vs Standalone Firms

We find that a greater proportion of FBGFs comply with the CSR law as compared to SFFs while the same holds true for OBGFs and NFs (Figure 6c). This can be plausible due to business group affiliated firms having better access to inputs such as talent, know-how and common internal institutions (Khanna & Palepu, 2000) that aid in implementing CSR programs faster and achieve better cost efficiencies than those without common shared resources.

Figure 6c: Proportion of Firms Meeting Prescribed CSR Norms



[31] PwC India Family Business Survey 2016 - https://www.pwc.in/assets/pdfs/publications/family-business-survey-2016/pwc-india-family-business-survey-2016-aligning-with-indias-growth-story.pdf

Bellwethers of CSR: State-Owned Enterprises

SOEs are found to be clearly outperforming other category of firms in our sample (Figure 6c). This can be attributed to the disparity in the legal framework governing central government-owned SOEs which were subject to mandatory CSR in the guidelines for Central Public-Sector Enterprises (CPSEs) published in 2010. As per the guidelines, such SOEs were already subjected to defined CSR budgets, which in some cases were more than the 2% CSR spend (Table 2).

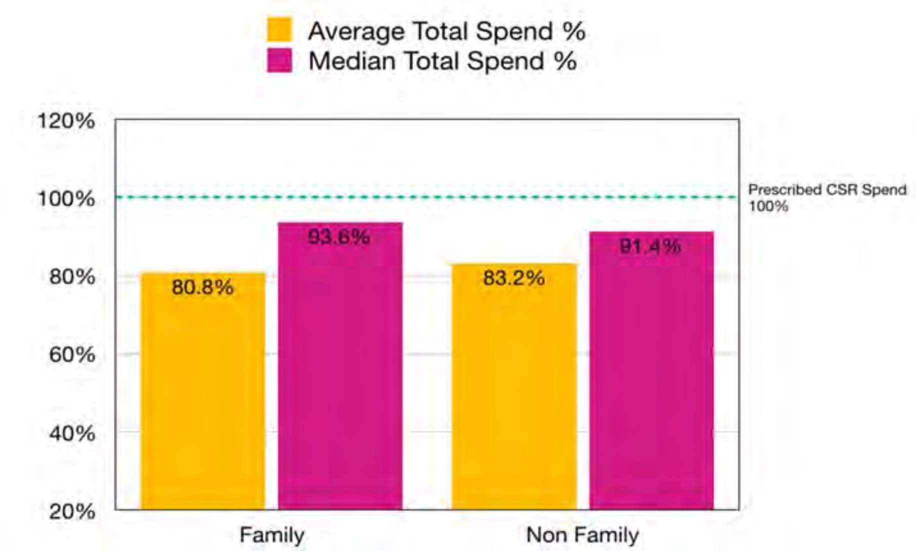
Table 2: CSR Guidelines for CPSEs in 2010

Profits	CSR Spend (as % of PAT)
Less than INR 100 crore (INR 1000 million)	3-5%
INR 100 - 500 crore (INR 1000 - 5000 million)	2-3%
More than INR 500 crore (INR 5000 million)	1-2%

Furthermore, these budgets were non-lapsable i.e. they had to be provisioned for spending in the subsequent financial years as per the DPE guidelines.[32] In case of other firms in our sample, the issue of carry forward of unspent amounts remained open to interpretation, till the time explicit clarity was provided in January 2016. It was provided that all companies including central government-owned SOEs, were *"free to decide"* on the carry forward of unspent funds.[33]

Consequently, at least partly, in our period of study, SOEs were subject to comparatively hard laws which created non-uniform regulations. Therefore, SOEs disproportionately affect the CSR contribution of non-family firms in our sample (Figure 7a & Figure 7b).

Figure 7a: CSR Spend by Prescribed Expenditure Across Three Years



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[32] Archive, Refer DPE guidelines revision of pg.18
https://dpe.gov.in/sites/default/files/Corporate_Social_Responsibility_Sustainability-Chapter-12.pdf

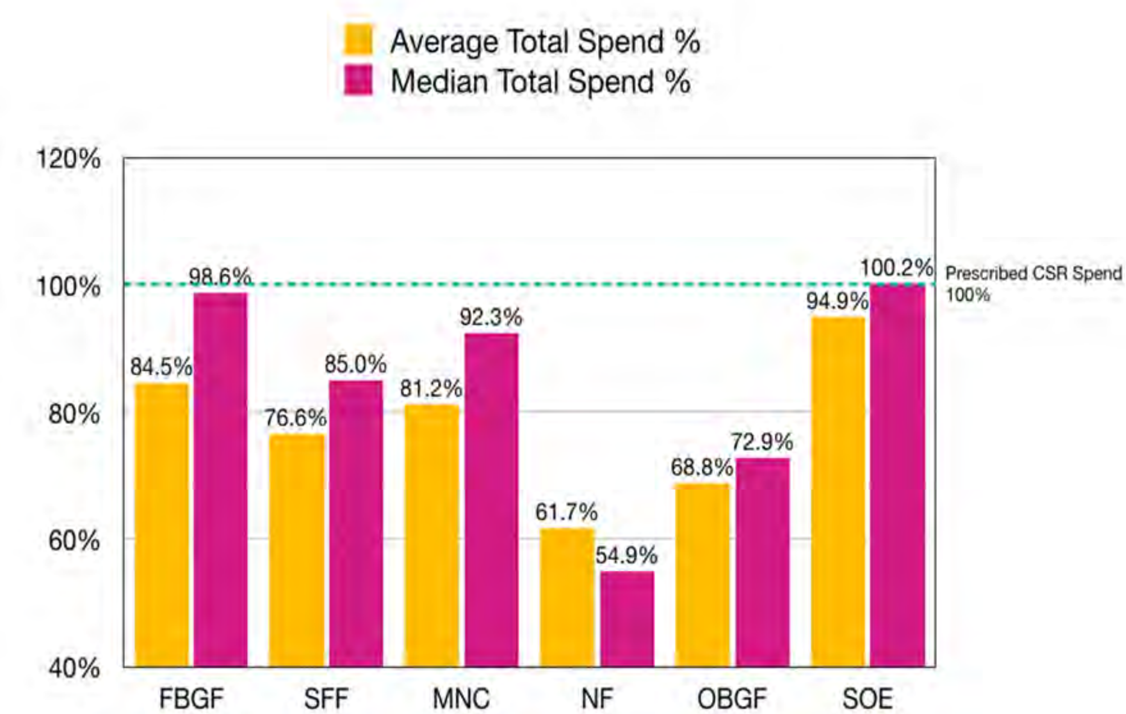
[33] Carry Forward of unspent CSR amounts: http://pib.nic.in/newsite/PrintRelease.aspx?relid=137505

Building Bridges: Multinational Companies

Our analysis shows that MNC compliance with mandatory CSR law has been higher (Figure 7b) than other non-family categories except for SOEs. The MNCs, when viewed from an institutional theory approach (Chapple & Moon, 2007), must not only keep in mind stakeholders in the local context but also those in the context of their parent company. Most of the MNCs operating in India have parent companies in the developed world where CSR is considered a norm. Further, they show a greater propensity in adapting to the institutional framework of CSR in the subsidiary's host country (Yang & Rivers, 2009) considering their foreign roots.

For instance, in gaining social legitimacy in the Indian context, especially considering India's colonial history which carries a suspicion and apprehension of foreign interests, it has become imperative that MNC executives undertake CSR initiatives (Balasubramanian et al., 2005). MNCs have imbibed that participation in social development should not merely be philanthropy led but an affirmative long-term initiative to build competitive advantages (Sundar, 2013). The enhanced intensity of marketing communication of their social initiatives allows them to capture the minds of India's growing middle class consumers while engaging in dialogues with the community to better understand their needs (Lattemann et al., 2009).

Figure 7b: CSR Spend by Prescribed Expenditure Across Three Years



The Curious Case of Widely-Held Professionalized Companies

It was observed that OBGFs and NFs are laggards in meeting their mandatory CSR obligations (Figure 7b). Our previous study, "Family Businesses: Promoters' Skin in the Game- 2001-2017", touched upon the characteristics of ownership structures in these firms. These firms have significantly lesser promoter shareholding with a higher concentration of non-promoter institutional shareholding[34].

In turn, the non-promoter institutional shareholders bring better corporate governance and financial knowledge in decision making process (Choi, Lee, & Williams, 2011) and reduce instances of corporate fraud and tunneling (Sharma, 2004). Further, it was established that such firms have strong formal internal control mechanisms to keep the personal interest out of the company's activities (Daily & Dollinger, 1992). We concluded by positing that the probability of strong and independent corporate governance mechanisms in the interest of shareholders would be higher in OBGFs and NFs.

Literature suggests that higher institutional investment, especially those with long-term horizons, leads to higher firm engagement in CSR as they are more concerned with firm's survival in the long run (Oh et al., 2011; Panicker, 2017). Moreover, they find that foreign institutional investors are positively aligned with CSR activities (Oh et al., 2011; Panicker, 2017) as they may emphasize socially responsible activities that are the norm in the context of developed countries. Considering the higher share of institutional shareholding especially of foreign nature in these companies, our results are not aligned with these findings, when strictly viewed from the broad ownership differences in our firm categories.

The behavior could perhaps be explained to some extent by the symmetric impact of corporate governance on CSR activities as found by other researchers. Arora & Dharwadkar (2011) provide that effective governance mechanism has a symmetric effect on CSR i.e. effective governance not only reduces non-compliance (bad CSR) in interest of firm's reputation but also curtails a proactive CSR approach (good CSR) - as independent directors, in acting as agents of shareholders, may be concerned only with economic returns and shy away from uncertain strategic investments such as CSR. Similarly, Jo & Harjoto (2011) also find support for the view that potential downside risks influence outside directors to support CSR activities at the firm level, however, they check on overinvestment by the managers who would want to enhance their personal reputation. While this argument explains that fewer OBGFs and NFs spend above the prescribed limit - it does not explain entirely why a vast majority of these firms are non-compliant.

Institutionalization of Values

In line with the stewardship theory (Miller & Le Breton-Miller, 2006), family firm managers in identifying with the organization's mission and vision, transfer enduring family values to the firm and act as responsible stewards in allocation of resources (Marques, Presas, & Simon, 2014; Lala, 2004). These values are in line with socially responsible behaviors such as altruism, collectivism, commitment, perpetuation and obligation. By corollary, non-family firms may not be

[34] Family Business: Promoter's Skin in the Game
https://www.isb.edu/sites/default/files/Family_Business_Promoters_skin_in_the_game_1.pdf

able to institutionalize these values and hence, not embed a culture of social obligation which results in higher CSR spending.

For instance, Biren Ramesh Bhuta, Chief CSR Officer at Tata Steel, a family firm in our sample, stated in an interview[35]: *"We do not look at 2% as a cut-off limit. The onus is on us to do more nuanced and high-impact activities to bring in social change. This is built into the DNA of our company. There are two compelling reasons: If you as a business want to survive for 100 years, you have to do right by the society you work in and if you want to grow, you cannot do so by leaving a large section of the society so behind"*

Anchored to 2% CSR spend?

Has the 2% mandatory spend by the law anchored CSR spending? Mindtree Limited recently faced shareholder opposition from non-promoter groups when it tried to pass a resolution to spend in excess of the prescribed limit.[36]

Press reports suggest this is the case with certain large companies that voluntarily spent amounts greater than the 2% limit in a bid to increase their corporate reputation but will now be compelled to recalibrate their social investments. Legal compliance is likely to take primacy in taking up any social welfare activities, and in turn, defeat the larger objective with which the law was enacted.[37]

Compliance Improving Over the Years

Year-wise breakup of CSR spending reveals that firms are incrementally increasing their CSR spending (Figure 8a & 8b).

The trends in our sample are in line with reports in the press which suggest that CSR spending increased by 27% in FY 2015-16[38] and 9% in FY 2016-17[39] for a sample of listed BSE companies. As a result, the overall unspent CSR amount has significantly decreased for our sample of firms from 2015 to 2017 (Figure 9).

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[35] https://www.livemint.com/Companies/oyHdaJdn96pnmzdIFUIFNO/How-companies-are-spending-on-CSR-projects.html

[36] https://www.livemint.com/Companies/9qac964t7mKQQkNOqfaImO/Mindtree-move-to-spend-10-profit-on-CSR-spurs-investor-deba.html

[37] https://www.theguardian.com/sustainable-business/2016/apr/05/india-csr-law-requires-companies-profits-to-charity-is-it-working

[38] https://www.thehindubusinessline.com/economy/csr-spend-rose-by-27-in-201516-cii/article9642346.ece

[39] https://cfo.economictimes.indiatimes.com/news/nearly-60-of-indias-funds-for-csr-are-spent-on-education-and-healthcare/63786203

Figure 8a: CSR Spend by Average Net Profit

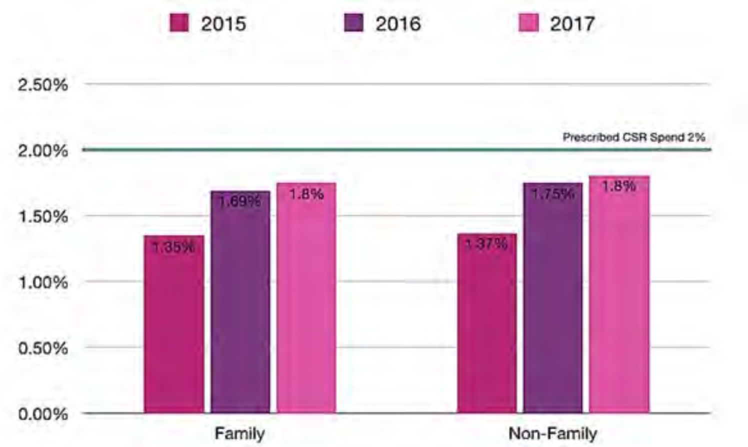


Figure 8b: CSR Spend by Average Net Profit

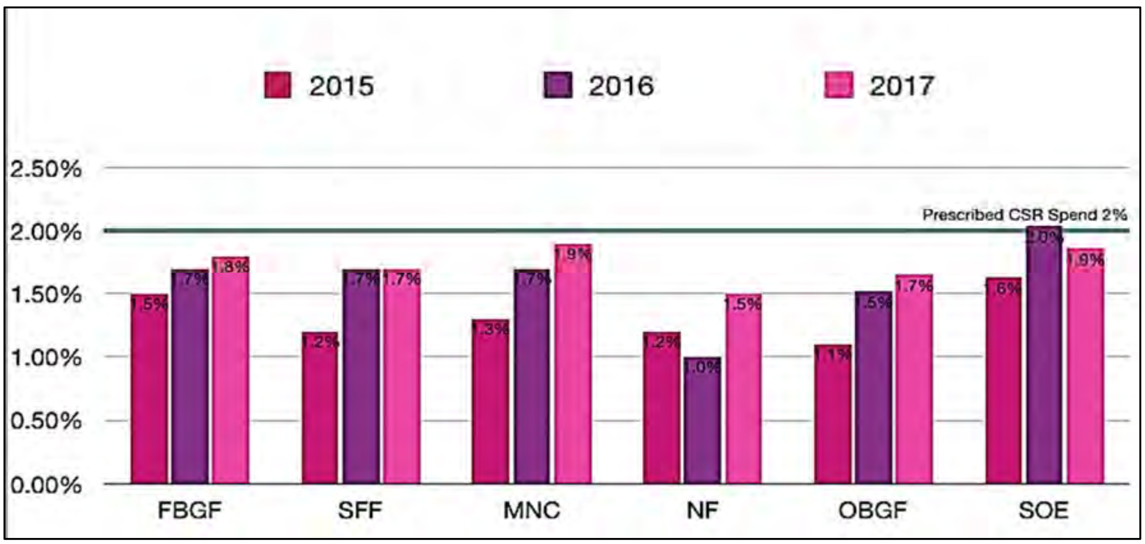
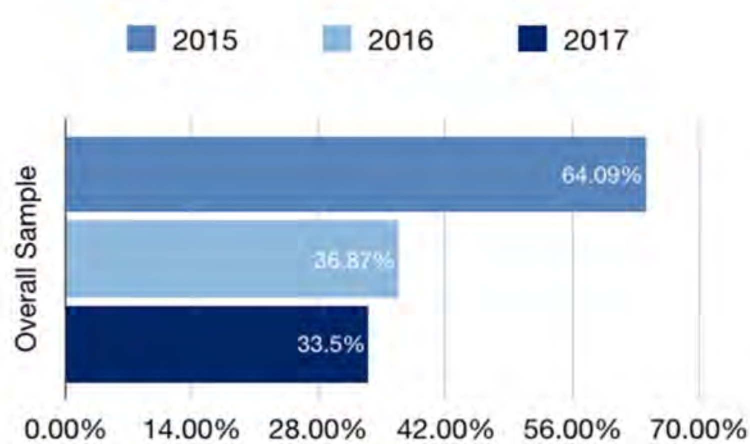


Figure 9: CSR Unspent % Amongst Non-Compliant Companies



5. Areas of Spend

The nature of spend of firms in our cohort can be understood in terms of the areas of spend referring to the development sectors favored by them. We juxtapose the choices made against what the law prescribes and understand possible reasons that defined behaviors for different categories of firms.

CSR Spends Not in 'Normal Course of Business'

The MCA released a notification in February 2014 with the final framework for implementation of the CSR law. Schedule VII had ten clauses[40] defined broadly across various development sectors such as education, healthcare, environment, rural development, women empowerment, art and culture, etc.

Further, it clarified that "CSR activities should exclude activities undertaken in normal course of business", which meant no firm could directly profit from the activities or gain goodwill by attaching its brand or name behind it.[41] Any activity that would benefit employees or their families was also not to considered as CSR spend[42]. This new framework hampered on the flexibilities that were earlier promised and was considered by corporate observers to be largely "prescriptive" in nature"[43].

Also, this framework brought the intent of the GOI to restrict CSR funds to a philanthropic context of community development activities as compared to larger global concept of CSR that includes incorporating responsible business practices into day to day operations focused on the wider theme of business responsibility and sustainability (Carroll, 1979). Surprisingly, the GOI had captured this wider understanding of CSR in the nine principles of the National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business released by MCA in 2011[44].

Nidumolu and Kallapur (2015) state that when CSR is "seen as a philanthropic activity, the company's key business groups do not consider CSR as integral to their activities. Instead, CSR becomes the responsibility of a separate group that is charged with such non-core activities. As a result, CSR activities do not benefit from the constant innovation and dynamism associated with mission-critical activities."

Understanding Schedule VII of the Companies Act, 2013

In June 2014, further clarifications to Schedule VII were provided which included,[45] (i) allowing a maximum of 5% of CSR spends for overheads and administrative expenses such as CSR staff salaries or volunteering time factored as monetary cost to the company (ii) implementing CSR activities in program/project mode and not as one-off events such as advertisements,

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[40] http://www.mca.gov.in/Ministry/pdf/CompaniesActNotification3_2014.pdf

[41] https://www.livemint.com/Companies/bAKkTMlOxdT5VZigmD7p3H/What-qualifies-as-CSR-and-what-does-not.html

[42] http://www.mca.gov.in/Ministry/pdf/CompaniesActNotification2_2014.pdf

[43] https://www.thehindubusinessline.com/companies/political-funding-kept-out-of-csr-ambit/article20732544.ece1

[44] http://www.mca.gov.in/Ministry/latestnews/National_Voluntary_Guidelines_2011_12jul2011.pdf

[45] http://www.mca.gov.in/Ministry/pdf/General_Circular_21_2014.pdf

sponsorships or charitable donations (iii) interpreting Schedule VII *'liberally'* so as to capture the essence of the subjects enumerated. It further added an eleventh clause to Schedule VII namely 'Slum area development'[46] (Figure 10).

Figure 10: Schedule VII of the Companies Act, 2013

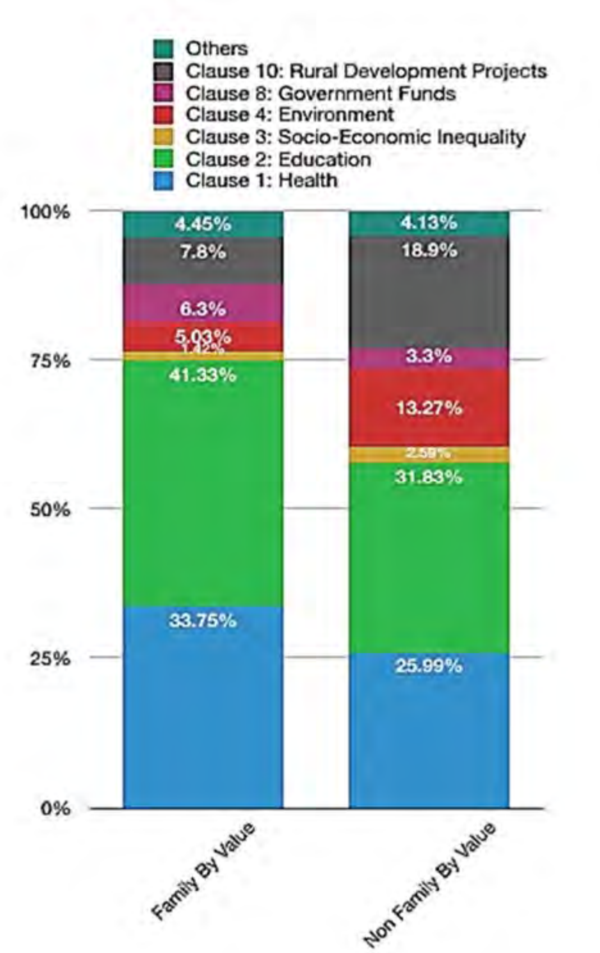
Clause	Areas of Spend
1	Eradicating hunger, poverty and malnutrition; promoting health care including preventive health care and sanitation including contribution to the 'Swachh Bharat Kosh' set-up by the Central Government for the promotion of sanitation and making available safe drinking water.
2	Promoting education, including special education and employment enhancing vocational skills especially among children, women, elderly, and the differently abled and livelihood enhancement projects.
3	Promoting gender equality and empowering women, setting up homes and hostels for women and orphans; setting up old age homes, day care centers and such other facilities for senior citizens and measures for reducing inequalities faced by socially and economically backward groups.
4	Ensuring environmental sustainability, ecological balance, protection of flora and fauna, animal welfare, agro forestry, conservation of natural resources and maintaining quality of soil, air and water including contribution to the 'Clean Ganga Fund' set-up by the Central Government for rejuvenation of river Ganga.
5	Protection of national heritage, art and culture including restoration of building and sites of historical importance and works of art; setting up public libraries; promotion and development of traditional arts and handicrafts.
6	Measures for the benefit of armed forces veterans, war widows and their dependents.
7	Training to promote rural sports, nationally recognized sports, Paralympic sports and Olympic sports.
8	Contribution to the Prime Minister's National Relief Fund or any other fund set up by the Central Government for socio-economic development and relief and welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women.
9	Contributions or funds provided to technology incubators located within academic institutions which are approved by the Central Government.
10	Rural development projects.
11	Slum area development.

[46] http://www.mca.gov.in/Ministry/pdf/lok_starred_ques_286_18122015.pdf

Distortions in Spending

Our study shows that Clause 1 and Clause 2 have been the most popular sectors for both family and non-family firms (Figure 11a & Figure 11b). On an average, nearly 60 percent of CSR funds are routed towards education and healthcare activities. Further, we find a heavy bias towards five clauses in our study - Clause 1: Healthcare and Sanitation, Clause 2: Education, Vocational Training and Skill Development, Clause 3: Environment, Clause 8: Government funds and Clause 10: Rural Development Projects which accounts for around 90% of CSR spend, in value, for all category of firms.

Figure 11a: Split by Clause % By Value



In a study on Indian philanthropy prior to the enactment of the CSR law, Mangaleswaran & Venkataraman (2013) had found similar results with education and healthcare receiving disproportionate amount of funds by donors. Some of the reasons stated by donors include personal association with deprivation in an area (in this case, education and healthcare); large gap in the current state vis-a-vis desired state in these sectors; lack of information, awareness and knowledge about other sectors of intervention; and the disproportionate supply of civil society organizations who operate in the education and healthcare sector.

Tax-Efficient CSR

When the legal framework for mandatory CSR came into effect in 2014, there was a lack of clarity if expenses under CSR would be eligible for deduction before computation of tax.[47] Subsequently, the GOI in a circular through the Central Board of Direct Taxes (CBDT) in January 2015 clarified that this would not be the case under the general deduction rule of Section 37(1). The reasoning provided by the GOI was that CSR expenses are an application of income that are not made in the normal course of business and would, therefore, be ineligible for any rebate. Further, the GOI clarified that tax deduction for CSR expenses would be akin to subsidizing one-third of the CSR expenditures, which would defeat the purpose of law.[48]

However, vestiges of the legacy Income Tax Act meant certain clauses under Sections 30 to 36 and Section 80(G)[49] created significant overlap between activities that could be tax deductible and construed as CSR activities under Schedule VII. This meant there existed a differential tax treatment of activities under the clauses.

The most popular sections for deduction were 35AC and 80(G)[50]. A report by Thinkthrough Consulting (TTC), shows that deductions claimed under Section 35AC increased by 421% from INR 143.5 crores in 2013-14 to INR 747.34 crores in 2014-15 (INR 1435 million to INR 7473.4 million). While under Section 80(G), the growth was a comparatively modest yet sizeable 96% growing from INR 1013 crores in 2013-14 to 1,985 crores (INR 10,130 million to INR 19,850 million) in 2014-15[51]. These stark increases indicate that most companies in our period of study would have favored activities that allowed the double benefit of being counted as CSR spend and providing tax rebate under the Income Tax Act.

Concerns with the differential tax incentives in the policy were also shared by the High-Level Committee (HLC) headed by Anil Baijal, which observed[52]:

"Differential tax treatment for expenditure on various activities covered under Schedule VII may create unforeseen distortions in the allocation of CSR funds across development sectors."

Deductions under Section 35AC have now been phased out as of April 1st, 2018 but other tax concessions continue to exist.[53]

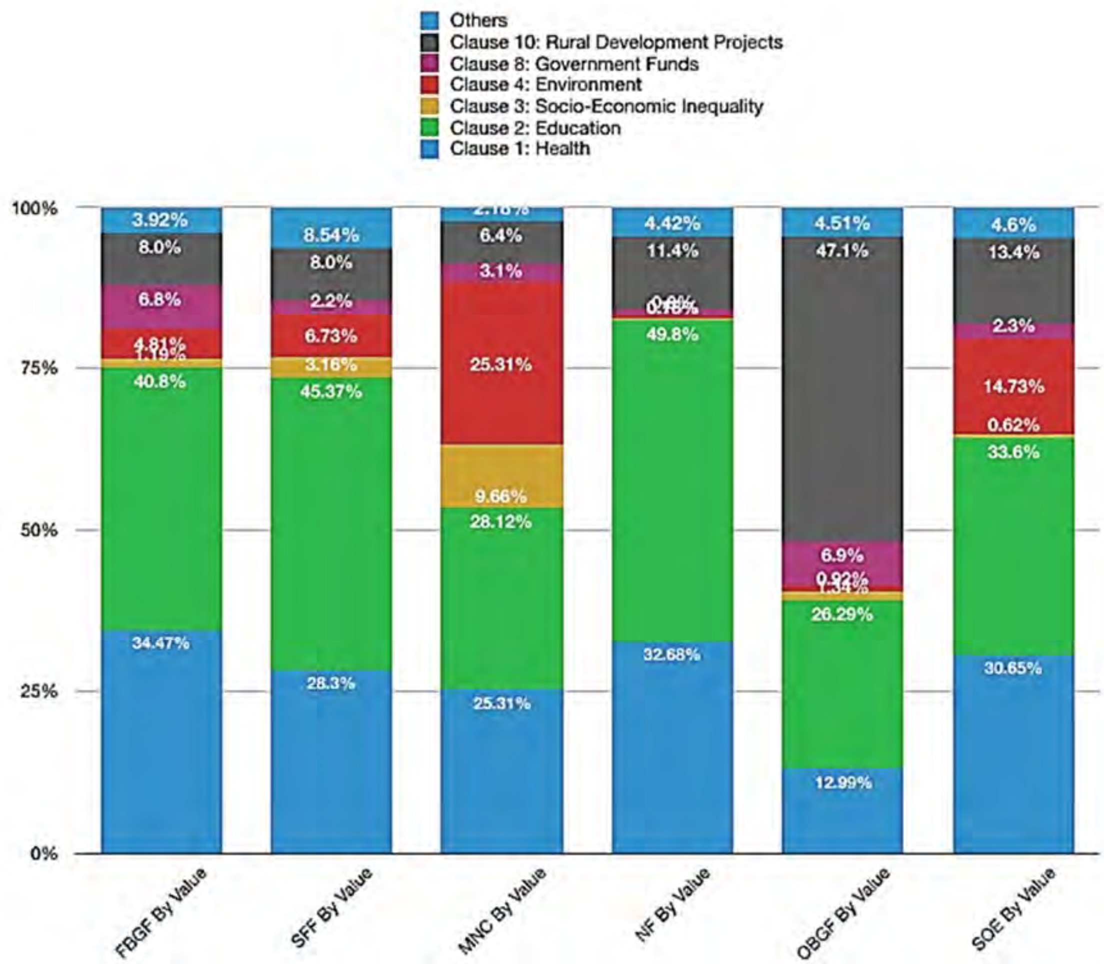
MNCs Aligned with Global Causes

Our study does find some interesting trends peculiar to our classification of firms. MNCs have invested a greater proportion of their funds into Clause 4: Environment and Clause 3: Socio-Economic Inequality (Figure 11b). A deep dive into MNC spending Clause 3 shows that 98% of that amount has been spent on 'women empowerment'. It is likely that this predisposition be

[47] https://www.financialexpress.com/archive/column-tax-twists-in-csr-spends/1231302/
[48] https://support.taxmann.com/pdf/circular/circular1_2015.pdf
[49] See Annexure 4 for more details on tax deductions available under the I-T Act
[50] https://www.financialexpress.com/opinion/columns-need-to-revisit-tax-norms-for-csr-spends/37259/
[51] https://www.livemint.com/Money/uPSK9Qrfo56g0KLtueOknL/Financial-gains-in-giving.html
[52] https://www.livemint.com/Politics/iTVm6yVLC1qKwWH3E6MxHP/Budget-2016-Review-the-varying-tax-for-CSR.html
[53] https://www.business-standard.com/article/pti-stories/deduction-benefit-under-section-35ac-only-till-march-31-116081900698_1.html

attributed to greater sensitivity towards climate change and gender equity that are part of a larger discourse in the western context and therefore, define the social consciousness of these firms[54].

Figure 11b: Split by Clause % By Value



Private Banks Leveraging CSR in Rural Areas

It is also observed that OBGFs in our sample contribute a large share of their CSR spends on Clause 10: Rural Development Projects (Figure 11b). Three companies within our OBGF categories include the largest private banks HDFC Bank, ICICI Bank and Axis Bank. Over the past decade, with rural economy growing on the back of government programs and increased consumption, these banks have rapidly increased their rural footprint to tap into the demand for different banking products.[55] In line with Porter & Kramer's (2006) concept of creating shared value through CSR, each of these banks has taken up dedicated village development CSR

[54] https://ssir.org/articles/entry/gender_equity_and_corporate_sustainability

[55] http://www.newindianexpress.com/business/2016/aug/06/Private-Banks-begin-revving-up-rural-branch-expansion-1505991.html

programs with a focus on increasing financial literacy and inclusion, thus, building a social dimension in their value chain and redefining their products and markets.[56,57,58]

In Response to the GOI's Call for Action

The GOI established funds with respect to its two flagship programs - "Swachh Bharat Abhiyan" and "National Mission for Clean Ganga". Contribution to these funds, called "Swachh Bharat Kosh" and "Clean Ganga Fund", were made eligible for CSR expenditures in Schedule VII. However, the GOI resisted temptations to make them tax deductible within the ambit of CSR spends by companies (otherwise they are 100% tax deductible), in keeping with the view that it would be perceived as influencing CSR towards a specific direction.[59]

We analyze how the introduction of these funds influenced behavior of firms in our sample. It can be observed that a very small share of CSR spends were allocated to these funds across our category of firms. Family firms were even less amenable to the GOI's call to action than non-family firms (Figure 12a). For every INR 100 spent on CSR programs, family firms spent only INR 0.20 as compared to INR 3.40 spent by non-family firms. While all categories of non-family firms consistently spent more than both categories of family firms on Swachh Bharat Kosh and Clean Ganga Fund, SOEs and OBGFs are markedly ahead in this respect (Figure 12b).

In line with increasing their socioemotional wealth, family firm members and managers are more likely to pick projects closer to their 'heart'. Most of these family businesses were first to set up charitable foundations and undertake strategic philanthropy through their foundations (Sundar, 2013), and as a result, they may have greater number of ideas to create social impact. In some well documented cases, family business promoters are more oriented towards giving back to the causes they are personally associated with especially in their ancestral communities and villages[60].

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[56] HDFC Bank - Holistic Rural Development Programme (HRDP) - https://indianexpress.com/article/business/companies/hdfc-banks-csr-initiative-meghalaya-village-becomes-750th-to-get-access-to-clean-water-4951660/

[57] ICICI Bank - Digital Villages Program - https://www.icicibank.com/csr/digital-villages.html

[58] Axis Bank - Village Social Transformation Mission - https://www.axisbank.com/docs/default-source/press-releases/axis-bank-foundation-joins-hands-with-government-of-maharashtra-to-transform-1000-villages.pdf?sfvrsn=6

[59] https://www.livemint.com/Politics/WqDfCMJOlsDufXftuDsyPP/Budget-2015-Tax-exemption-may-not-make-difference-to-Swachh.html

[60] https://www.outlookbusiness.com/specials/the-worlds-greatest-philanthropists/the-shape-of-things-to-come-1096

Figure 12a: Split by Government Flagship Program Funds

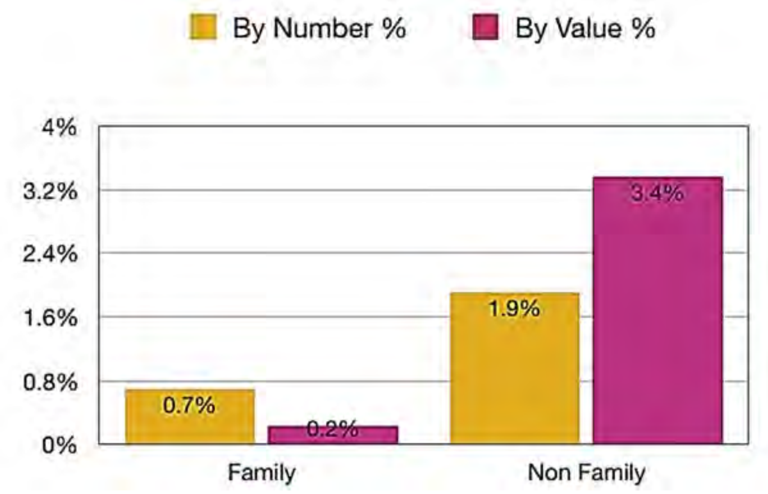
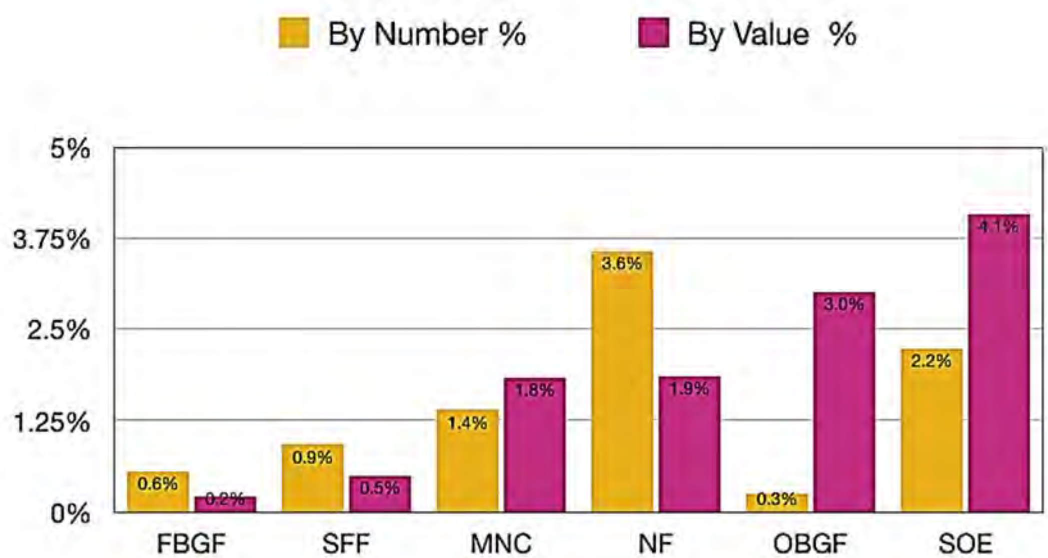


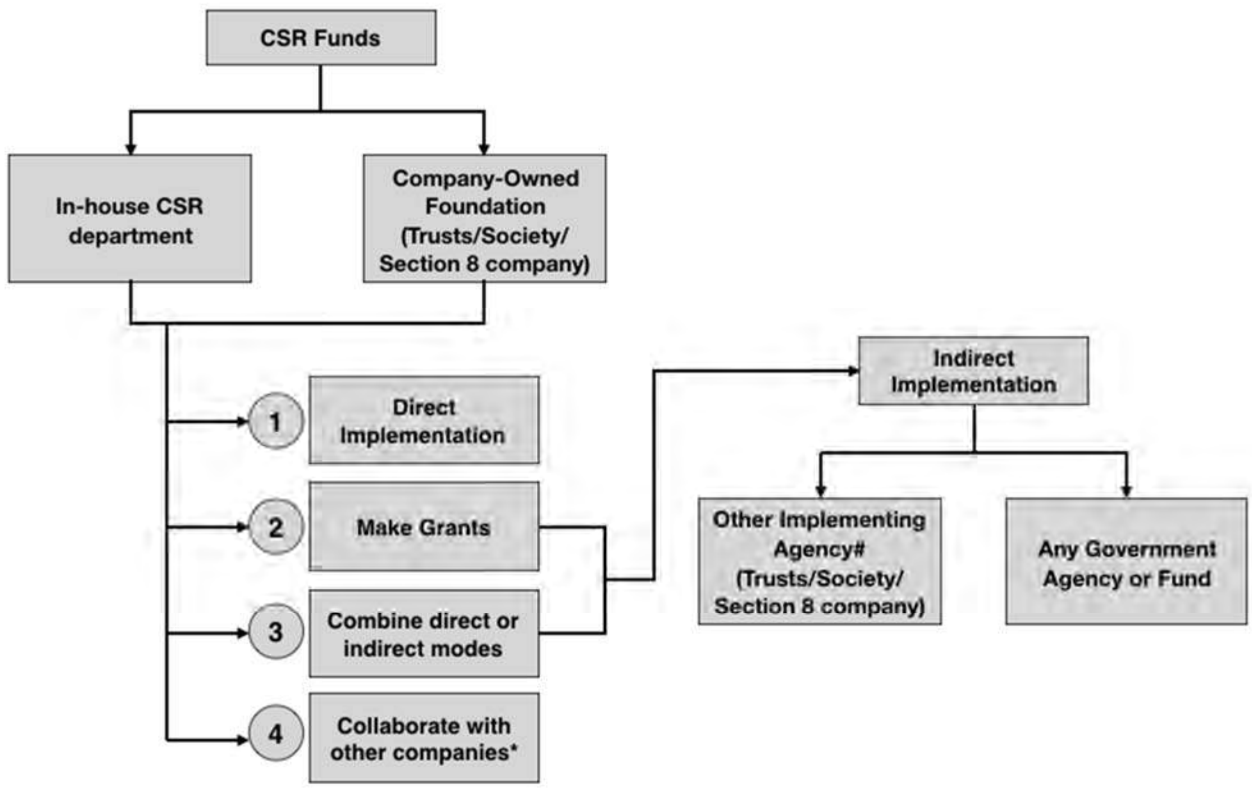
Figure 12b: Split by Government Flagship Program Funds



6. Mode of Implementation

In this section, we explore the preferred mode of implementation for our firms corresponding to the law. The final framework for CSR also provided for the modes in which the Company could implement their projects[61] (Figure 13).

Figure 13: Modes of Implementation



*if company can keep track and monitor the use of its funds
i) Entities should have an 'established track record' for a period of at least 3 years
ii) Company should specify use of funds and establish monitoring and reporting mechanism

Family Firms Prefer Greater Control on CSR Spends

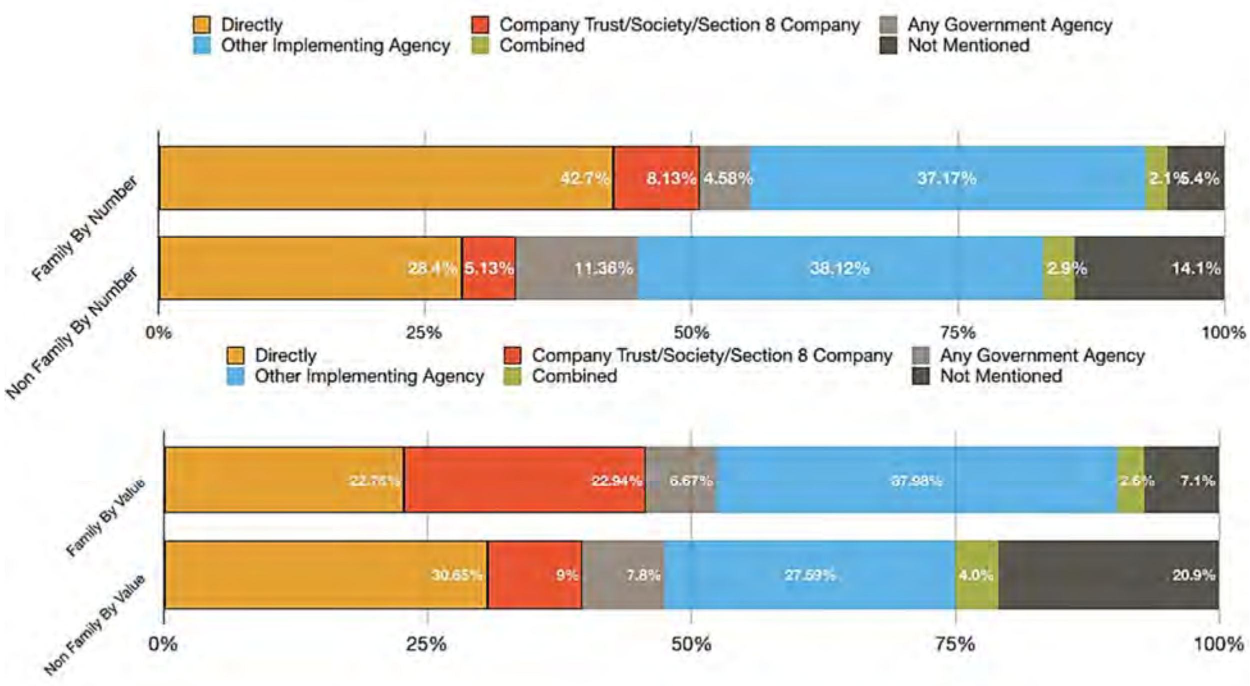
Our study shows that family firms are more likely to follow direct modes i.e. through the CSR department of the company or through the foundations established by the companies as compared to non-family firms (Figure 14a). In the Indian context, company owned foundations are typically not known for practicing arms-length philanthropy as compared to the Western foundations such as Bill and Melinda Gates Foundation, Ford Foundation and Rockefeller Foundation which are run by professional managers at the helm (Sundar, 2013). The promoters

[61] http://www.mca.gov.in/Ministry/pdf/CompaniesActNotification2_2014.pdf

in India exert significant influence over the foundation maintaining control of funds and the projects undertaken. This leads to principal-principal agency cost, especially in the case of concentrated ownerships (Dharwadkar et al., 2000; Morck et al., 2005; Young et al., 2008).

The principal-principal agency cost posits that financial value is expropriated from minority shareholders to the majority shareholders, which in this case is the family. Studies by Anderson & Reeb (2003) and Gómez-Mejía et al. (2007) show that this is pertinent to the social dimension as well. Families, in having direct control over the foundations, could expropriate resources to further their personal reputation and legacy in deploying CSR funds over the economic or strategic considerations of CSR for the business.

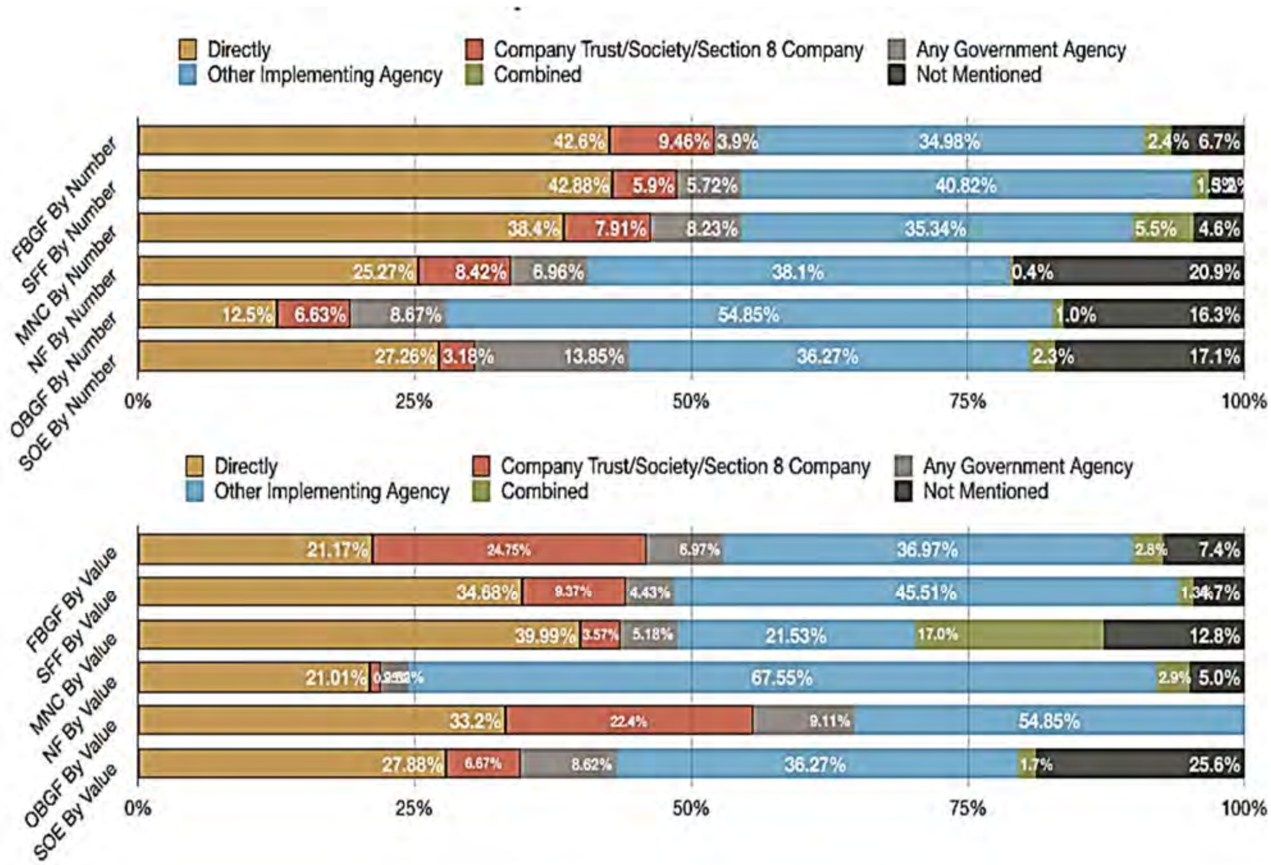
Figure 14a: Split by Mode of Implementation in %
i) By Number of Projects ii) By Value



Our analysis further shows that FBGFs and OBGFs spend appreciable amounts of CSR funds through their grant-making foundations when compared to the number of projects allocated (Figure 14b). While the non-economic utilities of enhancing the promoter's reputation and status can be attributed to FBGFs, OBGFs have stronger governance mechanisms to mitigate agency costs and are possibly more concerned with the economic considerations of cost efficiencies and tax benefits the company-owned foundation provides.

On the contrary, SFFs are more likely to spend their CSR funds directly through the in-house CSR team just as the MNCs (Figure 14b). Evidently, the incentives of having company-owned foundations diminish for these firms which operate in a standalone manner considering the legalese involved in setting up such a foundation. However, MNCs are more likely to combine multiple modes of implementation which shows a more direct involvement with local implementation partners in different geographies in implementing their strategic programs. (Porter & Kramer, 2006).

Figure 14b: Split by Mode of Implementation by %
i) By Number of Projects ii) By Value



Charitable entities registered under Section 80(G) and Section 35AC of the Income Tax Act[62], which provide 50% and 100% tax rebate respectively can be expected to have, to some degree, influenced the implementation modes adopted by the firms in our sample. In fact, contributing CSR funds to the corpus of companies' own foundation provided these tax benefits, contingent on their foundations being registered under Section 80(G) and the company, subsequently, choosing to avail the tax benefit.

[62] View list of tax exempted insitutions - https://www.incometaxindia.gov.in/Pages/utilities/exempted-institutions.aspx

Who Will Watch the Watchmen?

Armah, et al. (2011) provide that a developing economy context could be rife with risks considering weak administrative processes. Further, Wang et al. (2016) find that if administrative mechanisms are weak it would create fertile grounds for diverting CSR funds to projects that are brimming with vested and personal interests or more egregious still, the tunneling of CSR monies towards graft to influence local political interests.

According to an Economic Times report[63], some promoters/managers have gone to the extent of cheating the system, by donating funds to charitable foundations that return the money in cash after deducting their commission. The report finds that the tunneling of funds are preferred through public trusts, which are not governed by a single nationwide law. To compound matters further, in the annual filings with the MCA in a form called AOC-4, all other financial statements are required to be audited by an independent external auditor except the annual report on CSR activities.

[63] https://economictimes.indiatimes.com/news/economy/finance/how-indian-companies-are-misusing-public-trusts-to-launder-their-csr-spending/articleshow/49474584.cms

7. Conclusions and Implications

The focus on the social performance of the company is now inevitable in the globalized economy that firms operate in. This paper has attempted to provide an overview of CSR behaviors of different classes of firms by ownership in India given the unique regulatory landscape prevailing in the country. The antecedents and motivation for CSR are different for each of the classes in our cohort and results exhibit heterogeneity in behaviors.

Family firms outperform Non-Family firms: Family firms are more driven by non-economic utilities and are therefore, more likely to contribute to social welfare activities in keeping with the objective of building an enduring organization as trustees of society's wealth. FBGFs have been outperforming SFFs which points us to the advantages that BG affiliated firms have due to central institutional mechanisms such as company-owned foundations that are dedicatedly used to find avenues for social investments.

Family firms need stronger governance: It is commonplace for company-owned foundations to be run by family members of the promoters. These create principal-principal agency costs. It raises the question of whether the family benefits at the cost of other stakeholders of the company. As a result, families will have to professionalize their efforts and contend with implementing greater transparency and monitoring mechanisms to lend greater credibility to their social initiatives.

State-Owned Enterprises lead CSR push: We observed that SOEs have been largely driving the CSR spends in India, unsurprisingly, in keeping with their social welfare mandate. Despite forming only 4.7 percent of our sample in terms of numbers, they contributed to 31.7 percent of the total CSR spending of the sample as compared to 46.4 percent of FBGFs contributing to 42.7 percent of the total spend. However, it is imperative that the GOI does not exhibit a double-standard with respect to CSR at the expense of other retail shareholders. The GOI had clarified in a circular that CSR was not intended to fund gaps in government schemes[64]. However, recent press reports show this is not the case.[65]

MNCs' quest for localization: MNCs show a propensity to meet their obligations to entrench themselves in the Indian ecosystem bringing with them a social consciousness driven by western ideals. Establishing trust in the local context remains crucial to their long-term success and they will have to temper their obligations in keeping with the aspirations of their employees, local communities and the government.

Widely-held firms myopic towards CSR: OBGFs and NFs have been restrained in their spending indicating that continuity in long-term vision and institutional values may be an issue in such firms. Professional managers may not have the required will to proactively drive social welfare activities. The short-term horizons of non-promoter shareholders in these companies could be driving the priorities towards economic returns at the expense of long-term social investments.

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[64] http://www.mca.gov.in/Ministry/pdf/FAQ_CSR.pdf

[65] https://www.financialexpress.com/industry/cpses-csr-funds-to-foster-most-backward-districts/1258648/

Implications for Policy Making

The mandatory CSR policy was enacted in an environment where there was growing clamor for companies to become socially responsible. Has the CSR policy achieved results to that end? Unarguably, there are more funds that are being redirected towards social programs in India now. As per reports, the spending jumped by nearly 161% from INR 3368 crore (INR 33,680 million) in 2013-14 (Rai & Bansal, 2014) to INR 8803 crore (INR 88,030 million) in 2014-15[66]. In 2015-16 and in the second year of the law, spending has further increased by 12% to INR 9882 crore (INR 98,820 million). But questions arise in terms of their effectiveness, efficiency, impact and sustainability which are lacking in the data.[67] Therefore, for policy makers, as evidenced by our study, a multitude of unresolved issues and doubts about the implementation of the law come to the fore.

Narrow outlook of CSR: By limiting the focus of CSR to a philanthropic agenda stymies the possibilities for firms to fully leverage long-term benefits of CSR. For companies that adopt a typical philanthropic approach, Nidumolu and Kallapur (2015) find that "the level of commitment is subject to the vicissitudes of short-term profits, senior management interest, societal attention to philanthropy, and other such factors that affect the CSR's impact negatively".

Inefficient CSR spending: Antiquated tax laws present another challenge with firms more likely to choose avenues that provide tax benefits, impinging on the spirit of the law. Experts also believe that in the ideal case, the CSR spends should be complementary to the GOI spends in a sector. With emphasis on the company to decide on areas of spending, there could be oversupply or undersupply of funds and as a result inefficient social outcome of the CSR law.[68]

Disincentive to go 'above and beyond' the statutes: Has the 2% defined spend created a disincentive for companies who were spending more than the prescribed limit? In drawing from Tversky and Kahneman's (1974) work titled "Judgment under Uncertainty: Heuristics and Biases", anchoring effect has shown that there is a tendency for human beings to be significantly influenced by initial information at the time of making decisions about estimating uncertain values to contextual questions. Promoters have an uphill battle in convincing shareholders of the strategic long-term value especially in cases where promoter shareholding is not concentrated.

Lack of monitoring mechanism: Our study finds that while CSR spending is improving over the years, sizeable portion of the companies remain non-compliant. It is alarming that even though they could adopt passive CSR options such as donating to the Prime Minister's National Relief Fund (PMNRF) and receive tax benefits, they failed to spend up to the prescribed limit.

Directors as trustees of the nation: The annual report on CSR activities is the only financial document that is not required to be externally audited as part of Form AOC-4 filing with the MCA. This has been identified as a lacuna in the policy[69] placing the burden of truth of the CSR activities on the directors of the company. Further, the MCA clarified in a circular that no role will be played by the government in forming an external monitoring or impact assessment mechanism to check the quality and efficacy of CSR expenditures. Instead, they passed this responsibility back to the

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[66] https://www.livemint.com/Companies/8wH0n9DvxPnMzNtTlaes5I/Firms-spent-Rs8803-crore-on-corporate-social-responsibility.html

[67] https://www.livemint.com/Opinion/1wIQwFPRyRckBMg5IugW1K/Why-the-CSR-law-is-not-a-success.html

[68] https://www.livemint.com/Opinion/1wIQwFPRyRckBMg5IugW1K/Why-the-CSR-law-is-not-a-success.html

[69] https://economictimes.indiatimes.com/news/economy/finance/how-indian-companies-are-misusing-public-trusts-to-launder-their-csr-spending/articleshow/49474584.cms

Board of Directors/CSR Committees, who have been entrusted with self-regulating the quality of their firms' social responsibility practices in addition to being custodians of shareholder wealth.

The Way Ahead

As per a circular released by the MCA on April 4th, 2018[70], and in line with pervasive non-compliance post the enactment of the law, it had constituted a Steering Committee to review the functioning of CSR enforcement and recommend a uniform approach under the law. This has resulted in the Centralized Scrutiny and Prosecution Mechanism (CSPM), albeit on a pilot basis, which has been sending out show cause notices through the local Registrar of Companies (RoC) to companies who have not met compliance and have either not reported reasons for non-compliance or reported reasons deemed unsatisfactory in their annual report.

The GOI would be served well to look towards the European Commission (EC)[71] for inspiration which "believes that CSR is important for the sustainability, competitiveness, and innovation of EU enterprises and the EU economy. It brings benefits for risk management, cost savings, access to capital, customer relationships, and human resource management." Taking the focus away from pure philanthropy, the EC further adds that "CSR should be company led. Public authorities can play a supporting role through a smart mix of voluntary policy measures and, where necessary, complementary regulation."

The launch of the CSR portal in January 2018 has been another step in the direction of greater corporate transparency in allowing for social audit of the CSR activities as per the GOI[72]. Mr. Arun Jaitley, the Finance Minister of India, while launching the CSR portal stated:

"It's now all open to public gaze (which) has its own advantages. There is a pressure to make sure that compliance takes place. Everyone realizes that if there is any impropriety, the possibility of it being detected is going to be very high"

As a result, the intent and effectiveness of CSR programs will now be firmly predicated on the strength of corporate governance mechanisms at the firms rather than the quantum of CSR spends alone. Family firms, as mentioned earlier, might strongly consider building arm's length practices to lend further credibility to their CSR initiatives that are in the long-term interests of their businesses.

In conclusion, the GOI needs to be mindful of the fact that any strong legal crackdown might lead to more anxieties for independent directors, especially those who sit on the CSR Committees. The year 2017 witnessed independent directors resigning en masse that does not bode well for corporate governance in India[73]. Professors Ramachandran & Ray opine that good governance cannot be legislated and instead is a product of teamwork between enlightened promoters and independent directors[74]. The onus falls back on the promoters to understand the long-term advantages of their social obligations and to leverage CSR in a scrupulous manner despite the deficiencies of the mandatory CSR legal framework.

[70] http://www.mca.gov.in/Ministry/pdf/OfficeOrderNews_06042018.pdf

[71] https://ec.europa.eu/growth/industry/corporate-social-responsibility_en

[72] https://www.business-standard.com/article/government-press-release/arun-jaitley-union-finance-and-corporate-affairs-minister-launches-national-csr-118011901267_1.html

[73] https://economictimes.indiatimes.com/news/company/corporate-trends/independent-directors-head-for-exit-doors-on-compliance-stress/articleshow/60977881.cms

[74] https://www.business-standard.com/article/opinion/promoting-good-governance-118062701210_1.html

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Appendix 1: Identification of Family Firms

In the literature, family businesses are generally classified based on ownership, management and succession or business continuity. Ownership was used in 79 percent of the studies, 53 percent used management control, 28 percent used directorship, 15 percent used self-identification, 9 percent used multiple generations and 7 percent used intra-family succession intention, as the criteria to define a family firm (Machek, Kolouchová, & Hnilica, 2015).

For the purpose of classifying a firm as a family firm or a non-family firm, the Thomas Schmidheiny Centre for Family enterprise, Indian School of Business, identifies a firm as family firm if the first condition of significant ownership is met and any one of the other two conditions are met:

a. An equity ownership above 20 percent by family members or family controlled firms as on March 31, 2016 or the last shareholding data available. The cutoff of 20 percent was deemed to be appropriate as it has been found that individuals/families are able to control companies with much lower shareholdings due to large number of other shareholders that are widely scattered or financial institutions as shareholders that are not interested in the management of the company (Bagchi A., 1967) [75].

b. Family member as chairman of the board, or two or more family members[76] in the board of the firm. Once it was established that a Family has more than 20 percent shareholding in a company, it was determined if the family also exerts management control on the company. Wherever the Chairman of the Board, the Chief Executive Officer (CEO), the Managing Director, or a person in the board of directors was also a promoter and member of the family holding more than 20 percent stake in the company, that company was considered to be a Family Business.

In cases where the information about the Board of Directors was not available or it was difficult to determine whether the individual is a family member or not, the Annual Report of the company and the website, especially the History section and the Team/Management/Leadership sections, was explored to gain clarity.

c. Multiple generations or multiple members of same generations, actively involved in business. If a classification could not be arrived at through conditions (a) and (b), then the website of the company, along with search on the internet to get more information about the company was explored. If steps (a) and (b) satisfactorily classify a company as family, then step (c) was not performed. But if there was ambiguity in step (b), as there were companies where a family owned more than 20 percent shares, but the company was managed by a non-family CEO or Managing Director, in such cases, whether the stake of the company was being passed on from one generation to the other and the members of the family were involved in the company as owners, even if it was not in a leadership role, was checked for.

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[75] No significant changes were observed when the ownership cutoff was relaxed to 15 percent or increased to 25 percent.

[76] Family members were many times identified using the 'surname' matching approach when any conclusive evidence of relationship was not available. See (Machek, Kolouchová, & Hnilica, 2015) for a primer on the approach.

Appendix 2: Ownership Classifications

Businesses in India are characterized by many differing ownership structures. Prior literature on BGs does not distinguish between family and non-family business groups. Similarly, the prior literature on family businesses either focus on business groups or family firms irrespective of whether they are a part of a group or not. BG affiliated firms are usually bound together by various multiple ties such as common ownership, directors, products, financial, or interpersonal ties. Moreover, there is typically a core entity or dominant coalition, offering common administrative or financial control, or managerial coordination among the member firms (Granovetter, 2005). We believe that the family firms that are not affiliated to any business group will behave differently than the group affiliated ones.

SOEs or public sector undertakings as they are commonly referred to in India, are legal entities that are created by the government in order to partake in commercial activities on the government's behalf. It can be either wholly or partially owned by a government and is typically earmarked to participate in commercial activities. Examples include Indian Oil, NTPC, ONGC, Coal India etc.

MNCs are firms that have entered India through foreign direct investment. These firms make investments through which they acquire a substantial controlling interest in a domestic firm or set up a subsidiary in a foreign country (Markusen, 1995). Examples include Nestle, Cadbury, Microsoft, etc.

Other Business group affiliated firms (OBGFs)- One key characteristic of Business Groups in the literature is ‘kinship’ amongst top management. Business groups affiliated family businesses are therefore BGs in the true sense and have been classified as Family Business group firms (FBGFs) in this study. The other firms that meet the criteria of business group affiliated firms to a large extent but the top management in the various affiliated firms are not related in any way have the ‘kinship’ that a family has missing. They are hence classified separately as OBGFs. Examples are the ICICI Group, IVRCL Group, Larsen and Toubro Group, among others.

BG affiliated firms which were SOEs or MNCs were classified under SOEs and MNCs, not under OBGFs. For example, the companies under the State Bank of India group would be a part of SOEs.

Standalone non-family firms (NFs) form the remaining set of firms in the dataset. These firms are usually characterized by distributed ownership and a high degree of professionalization. Examples include Infosys, ITC, Global Trust Bank Ltd. etc.

SFFs are family firms that are not part of a business group.

Appendix 3: Prescribed Format for Annual Report on CSR

Extract of the Prescribed Format for Annual Report on CSR Activities (MCA)

1) A brief outline of the company's CSR policy, including overview of projects or programs proposed to be undertaken and a reference to the web-link to the CSR policy and projects or programs
2) The Composition of the CSR Committee
3) Average Net Profit of the company for last three financial years
4) Prescribed CSR Expenditure (two per cent. of the amount as in item 3 above)
5) Details of the CSR spent during the financial year
    a) Total amount to be spent for the financial year;
    b) Amount unspent, if any;
    c) Manner in which the amount spent during the financial year is detailed below

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Sl No.	CSR Project or Activity defined	Sector in which the project is covered	Projects or Programs 1) Local Area or other Specify 2) Specify the State and district where the projects or programs was undertaken	Amount Outlay (budget) project or programs wise	Amount spent on the projects or programs Sub Heads: 1) Direct expenditure on projects or programs 2) Overheads	Cumulative expenditure	Amount spent: Direct or through implementing agency

*Give details of implementing agency

6) In case the company has failed to spend the two per cent of the average net profit of the last three financial years or any part thereof, the company shall provide the reasons for not spending the amount in its Board report
7) A responsibility statement of the CSR Committee that the implementation and monitoring of CSR Policy, is in compliance with CSR objectives and Policy of the company.

Appendix 4: Tax Deductions Available

SI No.	Particulars	Tax Deduction	CSR Clause
1	Contribution to trusts/societies/foundations registered under Section 80(G)	50%	Multiple Clauses
2	Contribution to PM Relief or any other specified Govt Fund under Section 80(G)	100%	Clause 8
3	Contribution to university, college or similar institution for scientific research under Section 35(1)(ii))	175%	Clause 2
4	Contribution to university, college or similar institution for social or statistical research under Section 35(1)(iii))	125%	Clause 2
5	Expenditure on eligible project and schemes under Section 35AC*	100%	Multiple clauses but largely focused on[77] Clause 1, Clause 2, Clause 3, Clause 4, Clause 10
6	Expenditure on skill development project - Section 35CCD	150%	Clause 2

as on April 1, 2018

[77] https://www.soschildrensvillages.in/getmedia/26b0ede0-dc58-406a-9961-6ad8c359fe1a/35-AC-Overview.pdf

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ABOUT THE CENTRE

The Thomas Schmidheiny Centre for Family Enterprise brings together faculty and practitioners from India and abroad with the broad aim of combining theory and practice to enhance research and innovation in the field.

Family businesses make a major contribution towards wealth creation, job generation, and increasing competitiveness in countries around the world. As such, the unique challenges and opportunities faced by them are rapidly becoming an important subject of management research.

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