

Directors as Trustees of the Nation? India's Corporate Governance and Corporate Social Responsibility Reform Efforts

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INTRODUCTION

Corporate governance and corporate social responsibility (CSR) reforms have become a major focus of governments and corporations over the past several decades. In the United States, for example, following the Enron scandal and the recent financial crisis, both government and private industry have become embroiled in debates about the role of corporate governance in causing such crises and the corporate governance solutions to prevent future crises. Similarly, some investor groups, employee groups, and corporations themselves have advocated for or undertaken numerous CSR efforts. These efforts focus not just on shareholder wealth maximization, but also on the broader impact of the corporation on its stakeholders.

These debates are not just occurring in developed economies. Countries around the world are engaging in rich and nuanced debates, and undertaking significant reforms in the corporate governance and CSR arenas. This Article focuses on the relationship between corporate governance and CSR reforms in India—the world's largest democracy and one of its largest economies. Illuminating the trajectory of corporate governance and CSR efforts in India provides important lessons for reform efforts in other countries.

Corporate law in India has been fundamentally transformed since the early 1990s. In conjunction with significant economic liberalization, the Indian government has introduced a series of corporate governance reforms aimed in part at creating a system of transparent, ethical, and accountable corporate functioning.¹ Early reforms sought to implement rules and practices that addressed traditional corporate governance concerns, in other words the relationship between firm managers and shareholders and the relationship among different groups of shareholders, particularly majority and minority shareholders.

These early reforms include mandatory corporate governance requirements for listed companies that the Securities Exchange Board of India (SEBI) introduced through the amendment of Clause 49 of the Listing Agreement of Stock Exchanges (Clause 49).² They also include nu-

1. For a detailed history of developments in Indian corporate governance, see Afra Afsharipour, *The Promise and Challenges of India's Corporate Governance Reforms*, 1 INDIAN J.L. & ECON. 33, 64–67 (2010) [hereinafter Afsharipour, *Promise and Challenges*]; Afra Afsharipour, *Corporate Governance Convergence: Lessons from the Indian Experience*, 29 NW. J. INT'L L. & BUS. 335 (2009) [hereinafter Afsharipour, *Corporate Governance Convergence*]; Rajesh Chakrabarti, *Corporate Governance in India—Evolution and Challenges* 20 (Jan. 17, 2005) (unpublished working paper), available at <http://ssrn.com/abstract=649857>.

2. CIRCULAR, SECURITIES AND EXCHANGE BD. OF INDIA, AMENDMENTS TO CLAUSE 49 OF THE LISTING AGREEMENT (Sept. 12, 2000), available at <http://www.sebi.gov.in/circulars/2000/CIR422000.html> [hereinafter AMENDMENTS TO CLAUSE 49 (2000)]; CIRCULAR, CORPORATE

merous attempts by the Ministry of Corporate Affairs (MCA) to rewrite the Indian Companies Act (1956),³ to improve corporate governance, and to modernize India's company law. Recent reforms, such as the MCA's Corporate Governance Voluntary Guidelines (2009) (Corporate Governance Guidelines) have been more voluntary in nature, with the aim of encouraging companies to adopt better corporate governance practices.⁴

More recently, not only has the Indian government implemented laws to address corporate governance matters, but it has also started addressing CSR. In 2009, in conjunction with the introduction of new corporate governance guidelines, the MCA also proposed groundbreaking Voluntary Guidelines for Corporate Social Responsibility (CSR Guidelines) in 2009.⁵ The CSR Guidelines attempt to capitalize on the long history of philanthropy by large Indian firms. There is a robust history of Indian companies stepping into areas where they believed the state was failing, such as in education, health, and rural development. For example, the Tata Trusts, which controls 65.8% of the shares of Tata Sons, the holding company of the Tata Group conglomerate, regularly uses its income to support social causes.⁶ The wealth that accrues from this asset supports an assortment of socially responsible causes, such as institutions of higher education, medical research centers, and rural sanitation projects.⁷ The CSR Guidelines also attempt to move beyond a philanthropic model of CSR to a more expansive view of CSR that envisions the integration of social and environmental issues into businesses' decisions, goals, and operations, and in interactions between corporations and their stakeholders.

Like India's corporate governance reforms, the government's recent CSR guidelines place much responsibility on corporate directors. India's CSR Guidelines, along with the government's various public statements, view directors from a Gandhian perspective as trustees with duties to

GOVERNANCE IN LISTED COMPANIES—CLAUSE 49 OF THE LISTING AGREEMENT (Oct. 29, 2004), available at <http://www.sebi.gov.in/circulars/2004/cfdcir0104.pdf> [hereinafter CLAUSE 49 (2004)].

3. The Companies Act, 1956, Acts of Parliament, 1956.

4. MINISTRY OF CORPORATE AFFAIRS, GOVERNMENT OF INDIA, CORPORATE GOVERNANCE VOLUNTARY GUIDELINES 2009 (Dec. 2009) [hereinafter CG GUIDELINES (2009)], available at http://www.mca.gov.in/Ministry/latestnews/CG_Voluntary_Guidelines_2009_24dec2009.pdf.

5. MINISTRY OF CORPORATE AFFAIRS, GOVERNMENT OF INDIA, CORPORATE SOCIAL RESPONSIBILITY VOLUNTARY GUIDELINES 2009 (Dec. 2009) [hereinafter CSR GUIDELINES (2009)], available at http://www.mca.gov.in/Ministry/latestnews/CSR_Voluntary_Guidelines_24dec2009.pdf.

6. See Bala N. Balasubramanian, *Governing the Socially Responsible Corporation—A Gandhian Perspective*, in ETHICS, BUSINESS AND SOCIETY: MANAGING RESPONSIBLY (Ananda Das Gupta ed., 2010).

7. *Id.*; see also *Our Commitment*, TATA TRUSTS, http://www.tata.com/ourcommitment/sub_index.aspx?sectid=i6eUTkvtRos= (last visited May 16, 2011).

shareholders, stakeholders, and society as a whole.⁸ Both the CSR Guidelines and expected changes to the Companies Act would place the onus on the board of directors to supervise a company's CSR policies and to provide public reports on such policies, including the amount of profits spent on CSR efforts.⁹

India's corporate governance and CSR reforms have both, in large part, pinned their hopes on independent directors. In the corporate governance realm, the reforms envision independent directors as serving both a monitoring function and an advisory function. But while the independent director model has much to recommend, and there is some evidence of the markets assigning a positive value to independent directors on boards of Indian companies, there are serious constraints to relying on this model in the Indian context. It is clear that without significant additional reforms, the independent director model will not fully address the most important corporate governance concern in India: the pervasive influence of controlling shareholders (in the Indian context these shareholders are commonly referred to as promoters).

This Article argues that the Indian government's corporate governance and CSR efforts, while laudable in some respects, are problematic in their approach to the governance of Indian companies and reflect a view of the ownership and governance of Indian companies that does not necessarily address the fundamental governance issues that arise in Indian firms. India's proposed corporate law reforms suggest imposition of detailed corporate governance rules without necessarily assisting directors in addressing the fundamental majority–minority agency problems of controlled companies. Moreover, India's proposed CSR guidelines may further hamper independent directors and exacerbate some of the problems that this Article discusses with respect to majority–minority agency costs.

This Article is organized as follows: Part I explores the ownership structure of Indian firms and the role of independent directors in the governance of Indian firms. Part II assesses India's corporate governance reform efforts, and addresses whether these efforts relieve the corporate

8. Gandhi's view of the ownership of capital was one of trusteeship motivated by the belief that society was essentially providing capitalists with an opportunity to manage resources that need to be managed on behalf of society in general. See MEERA MITRA, IT'S ONLY BUSINESS! INDIA'S CORPORATE SOCIAL RESPONSIVENESS IN A GLOBALIZED WORLD 20–25 (2007). In a recent 2010 interview, the chairman of the MCA stated that directors and senior management are “custodians of public money, they are the trustees—if we go to the Mahatma Gandhi concept of trusteeship They are actually the trustees of the nation.” Interview by Jitendra V. Singh with R. Bandyopadhyay, Chairman, Indian Ministry of Corporate Affairs, available at <http://knowledge.wharton.upenn.edu/india/article.cfm?articleid=4488>.

9. See *CSR in India: Govt not to set CSR Floor for India Inc*, INDIA CSR, Dec. 25, 2010, <http://www.indiacsr.in/article-1760-CSR-in-India-Govt-not-to-set-CSR-floor-for-India-Inc.html>.

governance concerns in Indian firms. Part III investigates the origins and development of CSR in India and assesses recent attempts to incorporate CSR into corporate law, particularly through imposing CSR-related obligations on independent directors. A brief conclusion follows.

I. OWNERSHIP AND THE ROLE OF THE BOARD

Corporate law scholars generally argue that the nature of corporate governance concerns differ based on the ownership structure of firms.¹⁰ While for publicly owned firms with diverse ownership the governance concern is primarily about the agency costs of management vis-à-vis shareholders, for firms with controlling shareholders the “fundamental concern that needs to be addressed by governance arrangements is the controlling shareholder’s opportunism.”¹¹ Additionally, in controlled family-owned entities, various family members often serve in executive management or board positions. Thus, minority shareholders of controlled entities are often concerned with self-dealing transactions and other types of expropriation or extraction of wealth (tunneling) by majority stockholders.¹² But minority shareholders generally have limited power to affect the activities of the controlling stockholder through contesting control, voting rights, or pressuring the board of directors.¹³ There is also some concern that the prevalence of pyramidal ownership by family business groups¹⁴ with considerable economic power can affect voting by minority shareholders and even institutional investors, due to such shareholders’ business ties with the group.¹⁵

A. Ownership of Indian Firms

Like other Asian countries, concentrated ownership dominates the Indian corporate landscape.¹⁶ Until relatively recently, Indian firms had

10. For an overview of the differences between controlled and non-controlled companies, see Lucien A. Bebchuk & Assef Hamdani, *The Elusive Quest for Global Governance Standards*, 157 U. PA. L. REV. 1263, 1281–85 (2009). See also John Armour et al., *What is Corporate Law? in THE ANATOMY OF CORPORATE LAW: A COMPARATIVE APPROACH* 31 (R. Kraakman et al. eds., 2d ed., 2009); Ronald J. Gilson & Jeffrey N. Gordon, *Controlling Controlling Shareholders*, 152 U. PA. L. REV. 785 (2003).

11. Bebchuk & Hamdani, *supra* note 10, at 1282.

12. See, e.g., Simon Johnson et al., *Tunneling*, 90 AM. ECON. REV. 22, (2000) (defining tunneling as the “transfer of resources out of a company to its controlling shareholder (who is typically also a top manager)”).

13. See Bebchuk & Hamdani, *supra* note 10, at 1281–83.

14. See Tarun Khanna & Yishay Yafeh, *Business Groups in Emerging Markets: Paragons or Parasites?*, 45 J. ECON. LITERATURE 331–73 (2007).

15. See Assaf Hamdani & Yishay Yafeh, *Institutional Investors as Minority Shareholders* 1, 3 (2010) (working paper), available at <http://ssrn.com/abstract=1641138>.

16. See Rajesh Chakrabarti, William Megginson & Pradeep K. Yadav, *Corporate Governance in India*, 20 J. APPLIED CORP. FIN. 59 (2008); Lee Kha Loon & Angela Pica, *Independent Non-*

little dependence on global capital markets for funds, as family business groups controlled the majority of large companies and financial intermediaries played minor roles in firm ownership. Even following economic liberalization, family-group ownership (and its accompanying control and conflicts of interest issues) remains a mainstay of India's corporate landscape.¹⁷ According to a 2006 study, nearly 60% of India's 500 largest companies were affiliated with family business groups.¹⁸ For companies on the Bombay Stock Exchange (BSE) Sensitive Index (Sensex), which represents the top thirty companies and accounts for nearly a fifth of the BSE's total market capitalization, nearly a third were family owned and controlled.¹⁹

Because of the ownership structure of Indian firms, controlling shareholders (i.e., promoters) play an important and pervasive role in Indian corporate governance.²⁰ A 2005 study of over 3,000 Indian companies found that nearly half the market capitalization of those companies was directly held by the promoters.²¹ This study additionally suggested that the actual holdings likely exceed half, given that promoter shareholding is often hidden in the form of other corporate bodies or individual shareholders. In one case, the address provided by a company for a non-promoter corporate shareholder actually turned out to be that of the company's chairman.²² Regardless of how frequent such hidden hold-

Executive Directors: A Search for True Independence in Asia, CFA INST. CENTRE FOR FINANCIAL MARKET INTEGRITY CODES, STANDARDS, AND POSITION PAPERS (2010), available at <http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2010.n1.1>.

17. Satheesh Kumar T. Narayanan, *Indian Family-Managed Companies: The Corporate Governance Conundrum*, 5 ICFAI J. OF CORP. GOVERNANCE 20 (2006), available at <http://unpan1.un.org/intradoc/groups/public/documents/apcity/unpan033971.pdf>.

18. See Chakrabarti et al., *supra* note 1, at 59.

19. Narayanan, *supra* note 17, at 40. In smaller listed companies on the BSE, which makes up the largest portion of listed companies, family members generally own more than 50% of the company's shares. See LALITA SOM, STOCK MARKET CAPITALIZATION AND CORPORATE GOVERNANCE 7 (2006).

20. Under Indian law, "promoter" and "promoter groups" are defined to include:

(i) the person or persons who are in overall control of the company, (ii) the person or persons who are instrumental in the formulation of a plan or program pursuant to which securities are offered to the public, and (iii) the person or persons named in the prospectus as promoters.

SECURITIES AND EXCHANGE BOARD OF INDIA (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS 2(1)(za) (Aug. 26, 2009), available at <http://www.sebi.gov.in/guide/sebiidcrreg.pdf>.

21. K.S. Chalapati Rao & Atulan Guha, *Ownership Pattern of the Indian Corporate Sector: Implications for Corporate Governance* 11 (Inst. for Studies in Indus. Dev., Working Paper No. 2006/09, 2006), available at <http://isidev.nic.in/pdf/wp0609.pdf>; see also Shaun J. Mathew, *Hostile Takeovers in India: New Prospects, Challenges, and Regulatory Opportunities*, 2007 COLUM. BUS. L. REV. 800, 833 (2007) (noting that as of December 31, 2006, average ownership percentage of BSE 500 companies was 49.55%).

22. Rao & Guha, *supra* note 21, n.20.

ings actually are, it is clear that concentrated ownership still dominates the Indian corporate landscape.

There has been some shift in the concentration of ownership of Indian firms, with non-promoter institutional investors, both Indian and foreign, making significant inroads in the ownership of large Indian firms.²³ It is much too early, however, to state that the ownership pattern of Indian firms has changed dramatically.

*B. The Role of the Board in Controlled Companies:
The Indian Experience*

1. The Role of Directors in Controlled Companies

Just as the corporate governance concerns in controlled entities may differ from those in widely held firms, the role of the board, and particularly the role of independent directors on the board, also has important nuances in controlled firms. For controlled entities, outside directors serve what have been seen as “two broad, and sometimes opposing, roles”: as (i) monitors of controlling shareholders that work on behalf of minority shareholders; and (ii) brain trust, consultant, or “strategic advisor to the controlling shareholder.”²⁴

In their monitoring role, outside independent directors can help address corporate governance concerns of controlled entities. The monitoring role of independent directors is particularly important in jurisdictions like India, where the legal rights of minority stockholders may be limited. In controlled entities, independent directors can help prevent business decisions that improperly benefit controlling stockholders at the expense of minority stockholders. For example, they can monitor related-party transactions, in which there is a controlling stockholder conflict of interest.²⁵ In addition, independent directors can help protect the interests of minority shareholders and reduce extractions by controlling shareholders through “publicizing, or threatening to publicize, majority share-

23. See Chakrabarti et al., *supra* note 16, at 62. *But see* Rao & Guha, *supra* note 21, at 18 (stating that institutional investor holdings are very small for many companies).

24. Vikramaditya Khanna & Shaun J. Mathew, *The Role of Independent Directors in Controlled Firms in India: Preliminary Interview Evidence*, 22 NAT'L L. SCH. OF INDIA REV. 35, 45 (2010); *see also* Donald C. Clarke, *Three Concepts of the Independent Director*, 32 DEL. J. CORP. L. 73, 80, 81 (2007).

25. *See* Clarke, *supra* note 24, at 81; Deborah A. DeMott, *Guests at the Table?: Independent Directors in Family-Influenced Public Companies*, 33 J. CORP. L. 819, 847 (2008); Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 STAN. L. REV. 1465, 1506 (2007); Khanna & Mathew, *supra* note 24, at 45.

holder abuses” even if the directors have limited power to decide important issues without consent of the controlling stockholder.²⁶

In controlled companies with significant family influence, independent directors may also help navigate “difficult questions that implicate family ties as well as business necessity, including management succession and external threats to the firm’s position and separate existence” and may help the board “focus on the corporation’s business despite the distracting influence or overhang of frictions internal to the founding family.”²⁷ Independent directors may also influence board action to be more formal, professional, and transparent, especially in family-controlled firms that can be tempted to operate informally.²⁸

Scholars have also recognized that in controlled entities, outside directors may serve as strategic advisors to the controlling shareholder.²⁹ Such directors may help controlling shareholders and management with business decisions, and may offer strategic business advice and links with other entities.³⁰ Some scholars have argued that while corporate governance norms have moved toward outside directors as monitors of controlling stockholders, “it would appear that the strategic advisory role may be more suited to the actual functioning of boards, given that few boards meet more than once every two months.”³¹

2. Independent Directors in India

How does the reality of Indian boards line up with the academic theory about the role of boards in controlled entities? As will be discussed in Part II, corporate governance standards in India have undergone fundamental changes over the last two decades. Publicly listed Indian companies are required to have boards composed primarily of directors that can be deemed as independent under the stock exchange governance rules. These rules not only require independent board members, but also envision an expansive monitoring role for such directors. While the legal rules have been put into place, it is not yet clear whether directors themselves envision an expansive monitoring role.

26. Clarke, *supra* note 24, at 81; *see* Bebchuk & Hamdani, *supra* note 10, at 1295; Khanna & Mathew, *supra* note 24, at 46.

27. DeMott, *supra* note 25, at 824.

28. *See id.* at 857–58; Khanna & Mathew, *supra* note 24, at 46.

29. *See* Khanna & Mathew, *supra* note 24, at 46; Clarke, *supra* note 24, at 81; Gordon, *supra* note 25, at 1514.

30. *See* Clarke, *supra* note 24, at 99–100 (noting that such outside directors are not always considered to be independent directors).

31. Khanna & Mathew, *supra* note 24, at 47; *see also* Lisa M. Fairfax, *The Uneasy Case for the Inside Director*, 96 IOWA L. REV. 127, 161 (2010) (arguing that informational asymmetries inherent in the role of independent directors may limit their ability to be effective monitors).

A broad survey of corporate governance practices of Indian firms found significant room for improvement in the function of independent directors. For example, Indian law does not currently require director nominations by an independent nominating committee of the board, thus directors are typically nominated by controlling stockholders. This nomination process allows the “appointment of friends or colleagues of promoters or controlling shareholders as nonexecutive/independent directors.”³² Therefore, there is concern that such directors may not be truly independent and may have “a sense of loyalty to the controlling shareholder, potentially rubber-stamping proposals and disregarding minority shareholder interests.”³³

In addition, once nominated, it is not clear that independent directors possess the skills or tools necessary to address oppression of minority shareholders by majority stockholders. Many independent directors lament that there is no formal training for directors, and worry that the lack of training and resources may undermine their effectiveness.³⁴

Several recent studies of independent directors in India confirm that the role of directors in Indian firms is still in a state of development. One particularly illuminating study performed a broad survey of and interviews with independent directors at leading BSE 100 companies in India.³⁵ Based on their preliminary results, the authors found that independent directors of such companies envisioned their role to be as strategic advisors to controlling stockholders, rather than as monitors representing the interests of minority shareholders.³⁶ In fact, most directors reported little communication or contact with minority shareholders.³⁷ Directors cited several reasons for not functioning in a monitoring role, including: the lack of time, resources, or training; concern that performing as monitors could undermine board collegiality and functioning; and the high potential for direct liability.³⁸

32. *Corporate Governance Review of Practice: A study of Corporate Governance Practices in Leading Corporates in India*, NAT'L FOUND. FOR CORPORATE GOVERNANCE, Dec. 2007, at 52, available at <http://www.nfcgindia.org/pdf/asci250808.pdf>.

33. Loon & Pica, *supra* note 16, at 1.

34. *See id.* at 3.

35. *See* Khanna & Mathew, *supra* note 24.

36. *See id.* at 38–39.

37. *See id.* at 39.

38. *See id.* at 37.

II. INDIA'S CORPORATE GOVERNANCE REGIME

A. Clause 49 and the First Phase of India's Corporate Governance Reforms

The needs of India's rapid economic growth drove the country's corporate governance reforms.³⁹ Large Indian firms and industry groups advocated for the adoption of corporate governance standards that mirrored standards in more developed countries in order to obtain access to foreign direct investment, institutional investors (both domestic and foreign), and global capital markets.⁴⁰ Beginning in the late 1990s, industry groups such as the Confederation of Indian Industry (CII) advocated for comprehensive corporate governance standards.⁴¹ While India's corporate governance reforms were initially spearheaded by corporate India, the government, through SEBI, responded relatively quickly to industry demand by adopting Clause 49.⁴²

The adoption of Clause 49, a seminal event in Indian corporate governance, established a number of governance requirements for listed companies with a focus on the role and structure of corporate boards, internal controls, and disclosure to shareholders. The reforms introduced by Clause 49 "closely aligned to international best practice at the time and set higher governance standards for listed companies than most other jurisdictions in Asia."⁴³ The hallmark of Clause 49 was the introduction of independent directors into the Indian corporate governance system. Clause 49 includes a requirement that all listed companies have independent directors and sets forth some specific duties and obligations for in-

39. For an overview of India's economic transformation since 1991, see ARVIND PANAGARIYA, *INDIA: THE EMERGING GIANT* 107 (2008).

40. See Vikramaditya Khanna, *Corporate Governance in India: Past, Present and Future?*, 1 *JINDAL GLOBAL L. REV.* 171, 182 (2009); Bernard S. Black & Vikramaditya S. Khanna, *Can Corporate Governance Reforms Increase Firms' Market Value: Evidence from India* 9 (Univ. of Mich. Law Sch., Olin Working Paper No. 07-002, Oct. 2007), available at <http://ssrn.com/abstract=914440>.

41. CONFEDERATION OF INDIAN INDUSTRY, *DESIRABLE CORPORATE GOVERNANCE: A CODE*, (1998), available at http://www.acga-asia.org/public/files/CII_Code_1998.pdf.

42. AMENDMENTS TO CLAUSE 49 (2000), *supra* note 2; CIRCULAR, *CORPORATE GOVERNANCE IN LISTED COMPANIES—CLAUSE 49 OF THE LISTING AGREEMENT* (Aug. 26, 2003), available at <http://web.sebi.gov.in/circulars/2003/cir2803.html> [hereinafter *CLAUSE 49 (2003)*]. The Listing Agreement with stock exchanges defines the rules and processes that companies must follow in order to remain listed companies on an Indian stock exchange.

43. *ASIAN CORPORATE GOVERNANCE ASSOCIATION, ACGA WHITE PAPER ON CORPORATE GOVERNANCE IN INDIA* 9 (2010), available at http://www.acga-asia.org/public/files/ACGA_India_White_Paper_Final_Jan19_2010.pdf.

dependent directors.⁴⁴ These reforms were phased in over several years, and now apply to thousands of listed Indian companies.

While Clause 49 introduced reforms that are quite laudable, it has come under some criticism by scholars and corporate governance experts. Despite much fanfare and threats of vigorous enforcement, even several years after its enactment, compliance with Clause 49 remains less than ideal. For example, a 2009 study found that “less than a fourth of all independent directors are really independent in the sense that they have no connection with the promoters.”⁴⁵ In addition, “more than 3,000 people who were on the boards of various companies on January 1, 2006 were re-designated as independent directors to comply with” Clause 49 and “in around 30% of the companies, promoters simply re-designated themselves—calling themselves non-executive chairmen meant their companies could get by with a smaller proportion of independent directors (one-third, instead of half).”⁴⁶ Moreover, Indian regulators have been less successful in enforcing Clause 49’s extensive standards than in establishing them. SEBI has brought few enforcement actions for breaches of Clause 49 and has not been particularly successful even for those actions that it has brought.⁴⁷

Clause 49 has also been criticized because it addresses agency costs between managers and shareholders—i.e., problems of dispersedly owned firms—rather than minority shareholder oppression that could result from the concentrated ownership structures in Indian companies.⁴⁸ Scholars have posited that some of the shortcomings of Clause 49 are due to the transplant of governance reforms adopted in the United States and the United Kingdom into the Indian context without a comprehensive analysis of Indian corporate structures.⁴⁹ In a recent article examining India’s corporate governance reforms and the ownership structure of Indian firms, scholar Umakanth Varottil has comprehensively demon-

44. For a detailed discussion of Clause 49’s independent director provision see Umakanth Varottil, *Evolution and Effectiveness of Independent Directors in Indian Corporate Governance*, 6 HASTINGS BUS. L.J. 281 (2010) [hereinafter Varottil, *Evolution and Effectiveness*].

45. *Clause 49, RIP?*, BUS. STANDARD, May 29, 2009, available at <http://business-standard.com/india/news/clause-49-rip/18/28/359478>; see also Prithvi Haldea, *The Naked Truth About Independent Directors* (2009), available at http://www.directorsdatabase.com/IDs_Myth_PH.pdf.

46. *Clause 49, RIP?*, *supra* note 45.

47. Afsharipour, *Promise and Challenges*, *supra* note 1, at 57–59.

48. See generally *id.*; Afsharipour, *Corporate Governance Convergence*, *supra* note 1; Umakanth Varottil, *A Cautionary Tale of the Transplant Effect on Indian Corporate Governance*, 21 NAT’L L. SCH. OF INDIA REV. 1 (2009) [hereinafter Varottil, *A Cautionary Tale*]; Varottil, *Evolution and Effectiveness*, *supra* note 44.

49. See, e.g., Afsharipour, *Corporate Governance Convergence*, *supra* note 1; Varottil, *A Cautionary Tale*, *supra* note 48.

strated that “due to the concentrated ownership structures in Indian companies, it is the minority shareholders who require the protection of corporate governance norms from actions of the controlling shareholders. Board independence, in the form it originated, does not provide a solution to this problem.”⁵⁰ In fact, even those arguing that listed companies in India “are well regulated” admit that “oppression and mismanagement will remain always and [will need] to be tackled carefully.”⁵¹

B. *The Second Phase of Corporate Governance Reforms*

India’s corporate governance reform efforts did not cease with adoption of Clause 49. The MCA, which is responsible for overseeing all Indian companies and administering the Companies Act, has made several attempts to undertake a comprehensive revision of the Companies Act (1956).⁵² The MCA’s attempts to revise the Companies Act were revitalized in 2009 following the massive accounting scandal at Satyam Computer Services.⁵³ The MCA’s revisions to the Companies Act have received extensive review by the Parliament but have yet to be enacted into law.⁵⁴ In conjunction with the overhaul of the Companies Act and as a response to the Satyam scandal, the MCA introduced the Corporate Governance Guidelines.

50. Varottil, *Evolution and Effectiveness*, *supra* note 44.

51. Pushkar Chandna, *Satyam Lessons and Corporate Reforms*, SULEKHA.COM (Feb. 13, 2010), <http://pushkarchandna.sulekha.com/blog/post/2010/02/satyam-lessons-and-corporate-governance-reforms.htm>.

52. The Companies Act, 1956, Acts of Parliament, 1956 (as amended) provides the general legal framework for companies in India, including governing the incorporation, functioning, and winding up of Indian companies. All registered companies in India, whether public or private, are governed by the Companies Act.

53. In January 2009, the Indian corporate community was rocked by a massive scandal involving Satyam Computer Services (Satyam), one of India’s largest information technology companies. The scandal was comprised of an aborted related-party transaction involving the company’s promoters that led to the uncovering of colossal fraud in the company’s financial statements, including balance sheet errors showing fictitious cash assets of over U.S. \$1 billion. See *‘It was like Riding a Tiger, Not Knowing How to Get Off Without Being Eaten,’* FIN. EXPRESS, Jan. 8, 2009, available at <http://www.financialexpress.com/news/it-was-like-riding-a-tiger-not-knowing-how-to-get-off-without-being-eaten/407917/>; Mandar Nimkar, *How Much is Satyam’s Stock Actually Worth?*, ECON. TIMES, Jan. 8, 2009, http://articles.economictimes.indiatimes.com/2009-01-07/news/27644211_1_chairman-b-ramalinga-raju-cash-and-bank-balances-satyam-computer-services; Heather Timmon & Jeremy Kahn, *Indian Company in a Fight to Survive*, N.Y. TIMES, Jan. 9, 2009, available at <http://dealbook.nytimes.com/2009/01/09/indian-company-in-a-fight-to-survive>.

54. It is expected that the Companies Bill will be further amended as a result of an August, 2010, report by the Standing Committee on Finance of Parliament which examined the 2009 bill in great detail. See STANDING COMMITTEE ON FINANCE, FIFTEENTH LOK SABHA, THE COMPANIES BILL, 2009, TWENTY-FIRST REPORT (Aug. 2010), available at http://www.icsi.edu/webmodules/linksofweeks/21_Report_Companies_Bill.pdf.

1. The Corporate Governance Guidelines

Following the massive accounting fraud at Satyam Computers, the MCA proposed the Corporate Governance Guidelines, a set of good practices that may be voluntarily adopted by Companies.⁵⁵ The Corporate Governance Guidelines address a myriad of corporate governance matters including: independence of the board of directors; responsibilities of the board, the audit committee, and auditors; secretarial audits; and mechanisms to encourage and protect whistleblowing. Like prior corporate governance reforms in India, the Corporate Governance Guidelines emphasize the role of independent directors.

The Corporate Governance Guidelines do propose important reforms to address the independence of directors and the ability of independent directors to monitor controlling stockholders. In order to address the influence of controlling stockholders on the director nomination process, the guidelines propose the establishment of a nomination committee, a majority of which will be independent directors, including its chairman, for evaluating and recommending appropriate candidates for directorships to the board.⁵⁶ The Corporate Governance Guidelines set forth important details regarding the manner in which the nomination committee ought to function, with a focus on objectivity and transparency.⁵⁷ Scholars have argued that while a nomination committee is a step in the right direction, given the concentration of ownership and voting power in Indian firms, the appointment of such a committee may not significantly protect the interests of minority stockholders.⁵⁸ Indeed, “the nomination committee will likely pick candidates who have the tacit acceptance of the controlling shareholders so that the successful outcome of election of such candidates is not in doubt.”⁵⁹

Given that the Satyam scandal involved a foiled related-party transaction, the Corporate Governance Guidelines also make some inroads into addressing related-party transactions.⁶⁰ The guidelines require that

55. See CG GUIDELINES (2009), *supra* note 4.

56. *Id.* § I.A.3.

57. See *id.*

58. See Umakanth Varottil, *India's Corporate Governance Voluntary Guidelines 2009: Rhetoric or Reality?*, 22(2) NAT'L L. SCH. OF INDIA REV. 1, 6 (2010) [hereinafter Varottil, *Rhetoric or Reality*].

59. *Id.*

60. For a general discussion of the governance failures arising from related-party transactions in controlled firms generally, see ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT (OECD), GUIDE ON FIGHTING ABUSIVE RELATED PARTY TRANSACTIONS IN ASIA, (Sep. 2009), available at <http://www.oecd.org/dataoecd/39/57/43626507.pdf>; Loon & Pica, *supra* note 16. For academic studies of tunneling and pyramiding among Indian business groups, see, e.g., Chakrabarti, *supra* note 1, at 12; M. Bertrand, P. Mehta & S. Mullainathan, *Ferretting Out Tunneling: An Application to Indian Business Groups*, 117 Q. J. ECON. 121, 126 (2002).

the audit committee of the board of directors: (i) should monitor and approve all related-party transactions, and (ii) should provide public disclosure about all related-party transactions that take place in a particular year.⁶¹ Scholars have noted that the recommendation that the audit committee approve and monitor related-party transactions “is a substantial step in providing checks and balances against extraction of value from the company by controllers and other insiders.”⁶² But such a step may not be sufficient to protect minority shareholders from expropriation since the audit committee is not required to be composed of only independent directors and since there is no requirement that minority shareholders approve related-party transactions.⁶³

Overall, reaction to the Voluntary Guidelines by Indian corporate law scholars has been mixed, with one noted scholar stating that, “while the Guidelines do contribute to enhancement of the existing corporate governance framework in significant ways, they fail to satisfactorily address some of the shortcomings in the prevailing regime that have surfaced in the recent past.”⁶⁴

2. Amendment of the Companies Act

Since shortly after the approval of Clause 49, the MCA has attempted to reform the Companies Act to reflect more rigorous corporate governance provisions for all Indian companies. To date, the MCA has commissioned two separate committees to examine the Companies Act with respect to corporate governance provisions.⁶⁵ The reports of these committees have led to proposed amendments to the Companies Act, although such amendments have not yet resulted in legislation.

The MCA’s most extensive revisions to the Companies Act were introduced in 2008 and 2009. After years of delay in attempts to amend the Companies Act, the Companies (Amendment) Bill was introduced in the Indian Parliament in October 2008.⁶⁶ But the bill failed to become law that year. On August 5, 2009, the Companies Bill (2009) was introduced in the Lok Sabha (the directly elected lower house of the Indian

61. CG GUIDELINES (2009), *supra* note 4, § III.C.ii.

62. Varottil, *Rhetoric or Reality*, *supra* note 58, at 10.

63. *See id.*

64. *Id.* at 3.

65. For a detailed history and analysis of the MCA’s various corporate governance related committees, see Afsharipour, *Corporate Governance Convergence*, *supra* note 1.

66. Press Release, Ministry of Corporate Affairs (India), Bill Intends to Modernize Structure for Corporate Regulation in This Country (Oct. 23, 2008), available at <http://www.pib.nic.in/release/release.asp?relid=44114>.

Parliament) in the same form in which it was presented in 2008.⁶⁷ Commentators were shocked that there were no substantive changes to the Bill, despite the Satyam scandal.⁶⁸ Like the 2008 bill, the 2009 bill was left on the table.

In August 2010, the Standing Committee on Finance of Parliament (SCF) examined the 2009 bill in great detail.⁶⁹ The committee has made numerous recommendations to address India's corporate governance shortcomings. According to the SCF's report, the MCA has accepted that some of the matters included in the 2009 Voluntary Guidelines, discussed below, should be included in a revised bill. These include the separation of the roles of chairman and chief executive, the attributes and tenure of independent directors, board evaluation, the appointment of auditors, and the rotation of audit partners and firms. In general, the SCF's recommendations vest even greater authority and responsibility in independent directors. In terms of guidance to the MCA for amending the Companies bill, the SCF set forth the following guiding principles: "role of Independent Directors to be distinguished from other Directors in terms of appointment, duties and liabilities; maintenance of a panel recommended for their appointment; independence criteria to be clearly delineated; [and that] the institution to be allowed time to evolve."⁷⁰ According to some commentators, "while it is not doubted that the existing system of independent directors requires further review and strengthening, the SCF's recommendations seem to go the other extreme in advocating a process which amounts to regulatory micromanagement of corporate boards."⁷¹

With respect to amendment of the Companies Act, there are ongoing debates as to how to best address potential minority stockholder oppression. For example, in a recent press release, SEBI announced that it will recommend that the MCA amend the Companies Bill "to disallow interested shareholders from voting on the special resolution of the prescribed related party transaction. This will protect small and diversified

67. See Chakshu Roy & Avinash Celestine, *Legislative Brief: The Companies Bill, 2009*, PRS LEGIS. RES. (Aug. 18, 2009), available at <http://www.prsindia.org/uploads/media/Company/Legislative%20Brief—companies%20bill%202009.pdf>.

68. Umakanth Varottil, *Companies Bill Reintroduced in Parliament*, INDIAN CORP. L. BLOG (Aug. 4, 2009, 2:44 PM), <http://indiacorplaw.blogspot.com/2009/08/companies-bill-reintroduced-in.html>.

69. See STANDING COMMITTEE ON FINANCE, *supra* note 54; Umakanth Varottil, *Parliamentary Standing Committee on Companies Bill, 2009*, INDIAN CORP. L. BLOG (Sep. 5, 2010, 2:25 PM), <http://indiacorplaw.blogspot.com/2010/09/parliamentary-standing-committee-on.html>.

70. STANDING COMMITTEE ON FINANCE, *supra* note 54, at 17.

71. Umakanth Varottil, *Independent Directors under the Companies Bill, 2009*, INDIAN CORP. L. BLOG (Sep. 16, 2010, 2:32 PM), <http://indiacorplaw.blogspot.com/2010/09/independent-directors-under-companies.html>.

shareholders in listed companies from abusive related party transactions.”⁷² Scholars describe this proposal as an important step because under current Indian law there is little restriction on controlling shareholder conflict of interest transactions. The Companies Act currently does not require shareholder approval for related-party transactions.⁷³ Some commentators have lamented, however, that SEBI did not impose such a restriction on listed companies which are subject to SEBI regulations.⁷⁴

C. Continued Shortcomings in Indian Corporate Governance

As apparent from the above discussions, despite significant development in Indian corporate governance laws and regulations,

what becomes increasingly apparent in India is that the reform process has not addressed, or effectively addressed, a key challenge at the heart of the governance problem, namely the accountability of promoters to other shareholders. For example, even though most listed companies have large controlling shareholders, typically a family, India has a notably weak regime governing related-party transactions. There is little protection of minority shareholders under India’s legal regime, and no opportunity under the law for independent directors or independent shareholders to approve large related-party transactions. Promoters have considerable freedom of action in undertaking such transactions. In this context, relying largely on independent directors (appointed by controlling shareholders), independent board committees and greater corporate disclosure as the primary mechanisms to check abuses of power by promoters and to safeguard the interests of minority shareholders is likely to prove weak and insufficient. Board reform is fundamentally important, and is a major issue of concern to investors, but it needs to be complemented by other regulations that directly address the relationship between controlling and minority shareholders.⁷⁵

A number of experts have offered suggestions to address the potential oppression of minority shareholders.⁷⁶ These suggestions include: (i) altering the nomination and appointments process for independent directors; (ii) changing the election of independent directors to give a greater role to minority shareholders; (iii) encouraging investor activism;

72. SEBI BOARD MEETING, *available at* <http://www.sebi.gov.in/press/2011/201124.html>.

73. See Umakanth Varottil, *The Concept of an Interested Shareholder*, INDIAN CORP. L. BLOG, (Feb. 8, 2011, 8:15 AM), <http://indiacorplaw.blogspot.com/2011/02/concept-of-interested-shareholder.html>.

74. *See id.*

75. ACGA WHITE PAPER ON CORPORATE GOVERNANCE IN INDIA, *supra* note 43, at 10.

76. *See, e.g.,* Varottil, *Evolution and Effectiveness*, *supra* note 44.

(iv) clarifying the advisory and monitoring role of independent directors; and (v) increasing the qualifications and commitments of independent directors.

One of the most recent and interesting set of recommendations has been put forth by the Asian Corporate Governance Association (ACGA).⁷⁷ The ACGA's goal is to help address critical corporate governance areas that thus far "remain to be addressed—particularly relating to the accountability of promoters (controlling shareholders), the regulation of related party transactions, and the governance of the audit profession."⁷⁸ According to the ACGA, the accountability of promoters to other shareholders is "a key challenge at the heart of the governance problem."⁷⁹ In order to increase this accountability, the ACGA presents a number of important reform suggestions including: (i) providing greater disclosure prior to meetings to better improve shareholder meetings and to empower institutional investors by providing for more systematic voting, and (ii) addressing related-party transactions by giving independent shareholders the power to approve large transactions and requiring the appointment of an independent financial advisory and an independent board committee to determine whether the transactions are fair and reasonable to all shareholders.⁸⁰

The CFA Institute's Centre for Financial Market Integrity has made similar recommendations to address the fundamental governance problems of controlled entities. The CFA Institute has recommended that minority shareholders who own a minimum threshold percentage of shares be given the right to directly nominate director candidates.⁸¹ It has also recommended that controlled firms adopt cumulative voting schemes so as to improve the ability of minority shareholders to nominate and elect board members.⁸²

As discussed in Part II.B, some of these recommendations have been taken into account in the MCA's recent Corporate Governance Guidelines. Other recommendations have also been addressed in the proposed overhaul of the Indian Companies Act. Overall, however, many experts have expressed concerns either about the shortcomings of the proposed changes to the Companies Act and, given the significant delays

77. See ACGA WHITE PAPER ON CORPORATE GOVERNANCE IN INDIA, *supra* note 43.

78. *Id.* at 5.

79. *Id.* at 10.

80. *Id.*

81. See Loon & Pica, *supra* note 16, at 37.

82. *Id.*

in the amendment of the Companies Act, about the likelihood that such changes will be incorporated into Indian law.⁸³

III. INDIA'S CORPORATE SOCIAL RESPONSIBILITY MODEL—THE INDIA WAY?

In 2009, in conjunction with the introduction of the Voluntary Guidelines and the proposed overhaul of the Companies Act, the MCA also proposed groundbreaking CSR Guidelines. The CSR Guidelines attempt to capitalize on the long history of philanthropy by large Indian firms. The Ministry's guidelines include a strong focus on ethics, which it tied back to Indian history and values. The guidelines also view directors from a Gandhian perspective—as trustees with duties to shareholders, stakeholders, and society as a whole. In fact, according to the head of the MCA, directors and senior management are: “custodians of public money, they are the trustees—if we go to the Mahatma Gandhi concept of trusteeship . . . they are actually the trustees of the nation.”⁸⁴

This Part begins by exploring the history of CSR by Indian firms. It addresses how the concept of CSR has developed in India. This Part then addresses the MCA's recent efforts to incorporate CSR into Indian corporate law, and the potential benefits and shortcomings of these efforts in light of the country's corporate governance struggles.

A. CSR by Indian Firms

1. India's CSR Roots

It is a commonly held belief that CSR initiatives in India are driven in part by cultural norms and history.⁸⁵ The images of Gandhi and his trusteeship model, Indian scriptural edicts, and long traditions of philanthropy are linked to modern CSR initiatives.⁸⁶ Yet there is also skepticism about culture as a driving force of CSR uptake.

In her book, *Stages of Capital*, Ritu Birla gives insight into India's charitable history that provides parallels to modern CSR initiatives.⁸⁷ The merchant class of old paid tribute to the king to get real advantages, in-

83. See Varottil, *The Concept of an Interested Shareholder*, *supra* note 73; Somasekhar Sundaresan, *Two steps back with related party deals*, BUS. STANDARD, Feb. 14, 2011, available at <http://www.business-standard.com/india/news/two-steps-backrelated-party-deals/425032>.

84. For Gandhi's view of the ownership of capital, see *supra* text accompanying note 8.

85. See Adam Sulkowski & Steven White, *Financial Performance, Pollution Measures, and the Propensity to Use Corporate Responsibility Reporting: Implications for Business and Legal Scholarship*, 21 COLO. J. INT'L ENVTL. L. & POL'Y 491, 491 (2010).

86. See generally Balasubramanian, *supra* note 6.

87. RITU BIRLA, *STAGES OF CAPITAL: LAW, CULTURE, AND MARKET GOVERNANCE IN LATE COLONIAL INDIA* (2009).

cluding commercial privileges, protection of trade routes, and exemption from duties.⁸⁸ In the same way, CSR can be motivated by a desire to gain benefits from the government, including less scrutiny. Like the pre-British kings, modern government may be less interested in the business motivations of merchant endowments.⁸⁹ British rule brought the legal concept of trusteeship, which Gandhi built upon.⁹⁰ During British rule, business groups began involving themselves with public social discourse.⁹¹

The concept of trusteeship developed further during India's independence movement. "Gandhi's view of the ownership of capital was one of trusteeship motivated by the belief that essentially society was providing capitalists with an opportunity to manage resources which need to be managed on behalf of society in general."⁹² This view of trusteeship has been called revolutionary. According to an Indian CSR expert:

[Gandhi's view] was revolutionary in the sense that it was not just a guide to business functioning in society; it was an integral part of a wider world-view of society itself It was also revolutionary because it rested on a complete reformulation and in a sense negation of the twin aspects of capitalism as we know it—namely, the aspects of private property and competition. It was also revolutionary because, it still envisaged a future society, which could (in Gandhi's view) emerge within the parameters of a market economy. . . . Most of all it was challenging because it tried to combine two opposites—despite being anti-market in its approach, it proclaimed itself as not being anti-business.⁹³

Some large Indian business houses have long focused on philanthropy and have within their business model a sense of a social mission. Many of India's largest conglomerates have set up active separate philanthropic funds and welfare programs or initiatives, not necessarily as a legal duty or responsibility, but as a form of charity meant to indicate the virtues of the company or the organization.⁹⁴ For example, two-thirds of all the profits made by Tata Group companies go into two charitable

88. *Id.* at 77.

89. *Id.*

90. *Id.* at 103–04.

91. *Id.* at 212–31.

92. Sunyoung Lee, *Corporate Social Responsibility in India*, OXFORD-ACHILLES WORKING GROUP ON CORP. SOC. RESP. (2008) available at <http://www.sbs.ox.ac.uk/achilles/downloads/research/India.pdf>. For a more detailed discussion of Gandhi's trusteeship model, see MITRA, *supra* note 8; see also Balasubramanian, *supra* note 6, at 8–9.

93. MITRA, *supra* note 8, at 20.

94. *Id.* at 34–36.

trusts that support an assortment of socially responsible causes, institutions, and individuals in a wide variety of areas.⁹⁵

2. India's Emerging CSR Practices

Over the past several decades, India began a shift from the philanthropic model of social responsibility that predominated the era before liberalization, to a more Milton Friedman-style approach that focuses on the shareholders, and finally to the currently popular stakeholder model of CSR.⁹⁶ The stakeholder model of CSR recognizes that companies have responsibilities to not only their shareholders, but also to their employees, customers, surrounding communities (including the environment), and society as a whole.⁹⁷ Some commentators even argue that CSR is on the rise in India, with many firms conducting education, health, employment, skill development, affirmative action, and rural development activities.⁹⁸ Nevertheless, it is likely more accurate to state that for many Indian firms, CSR, particularly a more stakeholder-oriented CSR model, is in the early stage of development.⁹⁹ The shift to the stakeholder theory is not universal in practice—Indian businesses “continue to prefer to fund trusts and foundations at [arm’s] length from the company rather than integrating [CSR] practices into their core business processes.”¹⁰⁰ After deregulation, voluntary CSR activities have contributed to reducing skepticism; “there is a definite trend towards perceiving the corporate CSR actions in a positive manner.”¹⁰¹

Recently, some management scholars have argued that there is something unique about Indian business ideas, management practices,

95. See Balasubramanian, *supra* note 6, at 10.

96. See Seema G. Sharma, Comment, *Corporate Social Responsibility in India: An Overview*, 43 INT’L L. 1516, 1521 (2009); see also Rashmi S. Malapur, *Changing Paradigms in Management* 5, 6 (Feb. 6, 2009) (unpublished working paper), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1338580.

97. See Christoph Lattemann et al., *CSR Communication Intensity in Chinese and Indian Multinational Companies*, 17 CORP. GOVERNANCE: AN INT’L REV. 426, 429 (2009). A broad vision of CSR recognizes a “firm’s obligation to protect and improve social welfare through various business and social actions and by ensuring equitable and sustainable benefits” for these various stakeholders. *Id.* at 427.

98. INDIA BRAND EQUITY FOUNDATION, *CORPORATE SOCIAL RESPONSIBILITY/HUMAN RESOURCE* (2010), available at http://www.ibef.org/artdispview.aspx?in=84&art_id=26104&cat_id=926&page=1.

99. Pallavee D. Panthry, *Companies Differ on Executing CSR; So Does the Resultant Effect on Their Global Brands*, ECON. TIMES, Sept. 12, 2010, <http://economictimes.indiatimes.com/Financial-Times/articleshow/6536251.cms>.

100. Adam J. Sulkowski, S.P. Parashar & Lu Wei, *Corporate Responsibility Reporting in China, India, Japan, and the West: One Mantra Does Not Fit All*, 42 NEW ENG. L. REV. 787, 792 (2008).

101. Mahabir Narwal & Tejinder Sharma, *Perceptions of Corporate Social Responsibility in India: An Empirical Study*, 1 J. KNOWLEDGE GLOBALIZATION 61, 72 (2008).

and corporate leadership, particularly in the domain of CSR.¹⁰² According to a broad survey of Indian executives, many Indian firms have a sense of a social mission and purpose. These executives do not see shareholder wealth maximization as their primary goal. Instead, “they take pride in enterprise success—but also in family prosperity, regional advancement, and national renaissance. When asked about their priorities, Indian executives ranked investor interests below strategy, culture, or employees”¹⁰³

Indian business executives advocate for CSR as a moral duty and goal, but they also “see the long-term business sense.”¹⁰⁴ One study concluded that there was a positive relationship between stock listing status and aggregate CSR; listed companies had higher levels of CSR efforts than unlisted companies.¹⁰⁵ The study also found evidence that listed companies perform better than unlisted companies.¹⁰⁶ It further found that companies that had more extensive CSR activities, taking into account various stakeholders, increased firm performance.¹⁰⁷

Some companies and commentators justify CSR as good business sense, as “tangible value creation that can be weighed equally for business and society.”¹⁰⁸ An employee-driven CSR program reportedly increases employee satisfaction and productivity, and also improves employee skills.¹⁰⁹ P.S. Narayan of Wipro states that increasing efficiency is the main reason to undertake CSR, pointing out that “the world’s most ethical companies are consistently the more profitable companies.”¹¹⁰ Wipro chairman Azim Premji believes Wipro should go green internally, estimating the global market for environmental products and services will be over \$2 trillion by 2020.¹¹¹ Ajay Gupta of ruralnaukri.com has partnered with many NGOs to bring jobs and training to rural India, stat-

102. See PETER CAPPELLI ET AL., *THE INDIA WAY* (2010).

103. Michael Useem, *Chief Mentor: The India Way*, WALL ST. J., June 24, 2010, <http://blogs.wsj.com/indiarealtime/2010/06/24/chief-mentor-the-india-way>.

104. Sulkowski, Parshar & Wei, *supra* note 100, at 797.

105. Supriti Mishra & Damodar Suar, *Does Corporate Social Responsibility Influence Firm Performance of Indian Companies?*, 95 J. BUS. ETHICS 571, 582 (2010).

106. *Id.* at 582.

107. *Id.* at 585.

108. Santhosh Jayaram & Ruby Thapar, *Trading Credits for Social Responsibility*, ECON. TIMES, Jan. 12, 2010, <http://economictimes.indiatimes.com/Opinion/Policy/Trading-credits-for-Corporate-Social-responsibility/articleshow/5434992.cms>.

109. Writankar Mukherjee, *India Inc Boosting Employee-Driven CSR Drive*, ECON. TIMES, July 30, 2010, <http://economictimes.indiatimes.com/news/news-by-company/corporate-trends/India-Inc-boosting-employee-driven-CSR-drive/articleshow/6234902.cms>.

110. Panthry, *supra* note 99.

111. *Wipro’s Azim Premji: ‘Ecology Is One of Our Big Bets for the Future,’* INDIA KNOWLEDGE@WHARTON (Jun. 17, 2010), available at <http://knowledge.wharton.upenn.edu/india/article.cfm?articleid=4486>.

ing that rural development can “provide momentum to the giant wheel of the economy.”¹¹² Indeed, the purchasing power of rural consumers is on the rise; the average spending rate on many consumer goods is growing more quickly than average in rural markets.¹¹³

Many businesses now actively trumpet the business case for CSR. ITC states that their CSR strategy centers on competitiveness, improving customer satisfaction, and improving worker productivity.¹¹⁴ The Tata Group credits CSR for: an enhanced corporate image and added brand value; customer satisfaction and loyalty; access to quality business partners; favorable access to capital markets; good relations with public authorities and the general public; improved financial performance; increased productivity, sales, and quality; increased ability to attract and retain employees; and the general confidence of customers, suppliers, employees, communities, investors, activist organizations, and other stakeholders.¹¹⁵ Others have echoed that the business case for CSR hinges on the stakeholder model.¹¹⁶

There is a strong relationship between a corporation’s commitment to CSR and employee perception of CSR.¹¹⁷ India is seen to be more “collectivist than Western countries, which may have an impact on the importance of CSR to the Indian employee.”¹¹⁸ As such, it is likely that the business case for CSR is not universal.¹¹⁹ An Indian employee’s perception of his or her company’s social responsibility is related to his or her pride in the company.¹²⁰ Pride has a direct effect on satisfaction, creating a reduced intention to leave and improving perceptions of career

112. *Ruralnaukri.com’s Ajay Gupta: ‘Rural Jobs can Provide Momentum to the Wheel of the Economy,’* INDIA KNOWLEDGE@WHARTON (Mar. 26, 2009), available at <http://knowledge.wharton.upenn.edu/india/article.cfm?articleid=4362>.

113. *MNCs in Rural India: At a Turning Point*, INDIA KNOWLEDGE@WHARTON (May 6, 2010), available at <http://knowledge.wharton.upenn.edu/india/article.cfm?articleid=4472#>.

114. C. V. Baxi & Rupamanjari S. Ray, *Corporate Social & Environmental Disclosures & Reporting*, 44 INDIAN J. INDUS. REL. 355, 361 (2009).

115. Sandipa L. Anand, *Social Responsibility Initiatives in Tata Group: Tata Motors & Tata Chemicals 7* (July 11, 2005) (unpublished working paper), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=754564.

116. M. Kanchan, *Weaving Social Responsibility with Business Strategy: A Case Study of South Indian Paper Mills*, 17 CORP. SOC. RESP. & ENVTL. MGMT. 169, 171 (2010).

117. Hakhu Rahul, *Corporate Social Responsibility—An Indian Perspective*, 3(6) ADVANCES MGMT. 42, 43 (2010).

118. Walter G. Tymon, Stephen A. Stumpf & Jonathan P. Doh, *Exploring Talent Management in India: The Neglected Role of Intrinsic Rewards*, 45 J. WORLD BUS. 109, 110 (2010); Pavlos A. Vlachos et al., *The Moderating Role of Job Satisfaction Facets on Customer-Facing Employees’ Reactions to Corporate Social Responsibility: Preliminary Results from India and the Netherlands*, 15, 29 (July 14, 2010) (unpublished working paper), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=161836.

119. Vlachos et al., *supra* note 118, at 28.

120. Tymon, Stumpf & Doh, *supra* note 118, at 117.

success.¹²¹ Actual career success is not as important as satisfaction with the organization in reducing intention to leave, possibly due to cultural factors.¹²² Indian employees may not place the blame on the organization if they do not achieve career success.¹²³ One study on customer-facing employees found that CSR and job satisfaction help with recruiting employees, but this is unhelpful when the company is concerned about the turnover rate.¹²⁴

A number of Indian corporations have also joined the United Nations Global Compact (UNGC), a business initiative for social responsibility. Interestingly, one study suggests that firms unaffiliated with the UNGC that engage in CSR spend a higher percentage of sales on CSR than those firms who are associated with the UNGC.¹²⁵ Many Indian firms view the UNGC from a learning and networking perspective; the UNGC “facilitates entry in the CSR arena within no time and at a minimum cost to firms.”¹²⁶ Some scholars have discounted the participation of Indian firms in the UNGC, finding that their participation has not brought any significant improvements in human rights, labor, environment, and corruption.¹²⁷ The number of children employed in the workforce is still around 12.6 million.¹²⁸ Most Indian firms do not monitor their emissions or attempt to set strict caps on pollution.¹²⁹ The overall corruption rate in India is still high; the myriad attempts to deal with corruption have had negligible impacts.¹³⁰

While CSR activities have been on the rise in India, they have not been undertaken without criticism and skepticism. Repeating Milton Friedman’s famous position, Orissa Finance Principal Secretary, JK Mohapatra, stated that individual self-interest serves societal welfare, though he softened his position by suggesting that corporations should “pursue self interest in an enlightened manner to serve society.”¹³¹ Others have commented that CSR in its current form is “mere image-manship,” used to “cloak cynicism and irresponsibility,” and that, in order to be effec-

121. *Id.* at 118.

122. *Id.*

123. *Id.*

124. Vlachos et al., *supra* note 118, at 32.

125. A. K. Sharma & Rupal Tyagi, *CSR and Global Compact: The Indian Perspective*, 9(3) IUP J. CORP. GOV. 38, 43 (2010).

126. *Id.* at 55.

127. *Id.* at 56.

128. *Id.* at 57.

129. *Id.*

130. *Id.* at 58.

131. Nageshwar Patnaik, *Experts Seek CSR Code for Private Sector*, ECON. TIMES, Aug. 16, 2010, <http://economictimes.indiatimes.com/news/economy/policy/Experts-see-CSR-code-for-private-sector-/articleshow/6320807.cms>.

tive, CSR must be delinked from philanthropy, and instead associated with “high standards in the core business of corporations in dealing with shareholders and clients and the communities they operate in.”¹³²

B. Incorporating CSR into Indian Corporate Law

Over the past several years, the Indian government has attempted to transform CSR activities from a collection of good citizenship/philanthropic activities undertaken by only the largest business houses to a way of doing business that involves the right combination of enhancing long-term shareholder value and protecting the interests of various other stakeholders (such as employees, creditors, consumers, and society at large). For example, in 2009, the government made it mandatory for public-sector oil companies to spend 2% of their net profits on CSR.¹³³ Currently, the government is considering regulating CSR in the private sector. The government had initially indicated that it would impose mandatory CSR expenditures of between 2%–5% of a company’s net profits.¹³⁴ Officials have been working on a way to quantify CSR.¹³⁵ The government has also been working to incorporate CSR standards into the amendment of the Indian Companies Act.

1. Corporate Social Responsibility Voluntary Guidelines (2009)

In the past year, the Indian government took steps to incorporate this broader vision of CSR into Indian corporate law. In late 2009, the MCA proposed groundbreaking CSR Guidelines in what has been deemed the first concrete attempt to recognize CSR from a regulatory standpoint.¹³⁶ The CSR Guidelines constitute the outcome of committee sessions conducted by the Indian Institute of Corporate Affairs (IICA) with Advisory Expert Group members of the IICA-GTZ CSR Initiative,

132. Swaminathan S. Aiyar, *Corporate Social Responsibility Can Cloak Irresponsibility*, ECON. TIMES, July 25, 2010, <http://economictimes.indiatimes.com/news/news-by-company/corporate-trends/Corporate-social-responsibility-can-cloak-irresponsibility/articleshow/6212519.cms>. It is also not clear that CSR activities have translated to greater support of charities. The *Wall Street Journal* reports that donations to charity by individuals and corporations are relatively low in India, possibly due to the inadequacies of the current tax deduction structure. Durga Raghunath, *Why Don't Indians Give More?* WALL ST. J., Apr. 26, 2010, <http://blogs.wsj.com/indiarealtime/2010/04/26/why-dont-indians-give-more>.

133. *Id.*

134. See Patnaik, *supra* note 131; INDIA BRAND EQUITY FOUNDATION, *supra* note 98.

135. INDIA BRAND EQUITY FOUNDATION, *supra* note 98; Jayaram & Thapar, *supra* note 108.

136. See Umakanth Varottil, *Voluntary Guidelines on Governance and Social Responsibility*, INDIAN CORP. L. BLOG (Dec. 31, 2009, 10:36 AM), <http://indiacorplaw.blogspot.com/2009/12/voluntary-guidelines-on-governance-and.html>.

a bilateral Indian/German project.¹³⁷ The guidelines themselves attempt to frame CSR as part of Indian history and culture, stating: “Indian entrepreneurs and business enterprises have a long tradition of working within the values that have defined our nation’s character for millennia. India’s ancient wisdom, which is still relevant today, inspires people to work for the larger objective of the well-being of all stakeholders.”¹³⁸

The fundamental principle of the CSR Guidelines is that

each business entity should formulate a CSR policy to guide its strategic planning and provide a roadmap for its CSR initiatives, and that this should be an integral part of overall business policy and aligned with a company’s business goals. The policy should be framed with the participation of various level executives and should be approved and overseen by the Board.¹³⁹

According to the CSR Guidelines, the CSR Policy should cover the following core elements: (i) care for all stakeholders, including shareholders, employees, customers, suppliers, project-affected people, society at large, etc.; (ii) ethical functioning, transparency, and accountability; (iii) respect for workers’ rights and welfare; (iv) respect for human rights; (v) respect for the environment; and (vi) activities for social and inclusive development.¹⁴⁰

While the guidelines have a very broad vision, they have a number of problems. The CSR Guidelines’ expansive and cursory treatment of many aspects of CSR does not assist companies to address where their CSR focus should be, and leaves much of this up to the corporations themselves. This is particularly problematic given the corporate governance shortcomings in India. Given the pervasive control of promoters in Indian firms, there is a danger that CSR will be reduced to a few philanthropic activities undertaken by the promoter. This could foster the continuation of a narrow view of CSR which does not necessarily translate to greater social responsibility to a company’s employees or to the environment.

The CSR Guidelines also provide little concrete guidance on how companies are to implement the guidelines or on what legal changes need to be made to ensure that socially responsible practices will be part of a firm’s way of doing business. It appears from the fundamental principle of the guidelines that the board of directors will formulate and ap-

137. See RESPONSIBLE BUSINESS, NATIONAL VOLUNTARY GUIDELINES ON SOCIAL, ENVIRONMENTAL AND ECONOMIC RESPONSIBILITIES OF BUSINESS (2009), <http://responsible-business.in/csr-guidelines>.

138. CSR GUIDELINES (2009), *supra* note 5, at 9.

139. *Id.* at 11.

140. *Id.* at 11–12.

prove CSR policies. Board members, however, may not have the knowledge or tools to undertake these efforts, but there has been little recognition of such shortcomings with respect to placing responsibility on directors to formulate and approve CSR policies.

In addition, similar to the corporate governance Voluntary Guidelines, the CSR Guidelines are, as the name indicates, just guidelines. There is little in terms of enforcement. This is arguably positive, as the CSR guidelines are just the initial step into regulating CSR activities. Indeed, some experts have argued that CSR requirements might benefit from a “voluntary approach with stringent disclosure requirements that induce a culture of ‘comply-or-explain.’ This would help vigilant investors, particularly socially responsible and ethical investors, to either engage with the companies to ensure they operate in a socially responsible manner or alternatively to exit such investments.”¹⁴¹

2. CSR and Amendment of the Indian Companies Act

In 2010, the MCA began to move toward incorporating CSR, and a more mandatory version of CSR, into the Companies Act. Thus far, the MCA has fluctuated between imposing mandatory CSR requirements into the Companies Act and adopting CSR recommendations with a “comply-or-explain” approach. Given the current inertia in actually passing the Companies Bill, it is not yet clear which vision will win out, although given the vehement opposition to consideration of mandatory requirements one would expect that the MCA will adopt a more voluntary approach.

In line with the thorough examination of the Companies Bill (2009) by the Standing Committee of Parliament on Finance, which includes a review of the extent of CSR being undertaken by corporations and the need for a comprehensive CSR policy, the MCA indicated that it would introduce CSR requirements into the Companies Bill. An MCA press release in mid-2010 indicated that the Bill may now include provisions to mandate that every company with a net worth of at least Rs.500 crore (about \$111 million), turnover of at least Rs.1000 crore (about \$222 million), or a net profit of at least Rs.5 crore (about \$1.1 million) during a year would be required to formulate a CSR Policy to ensure that every year at least 2% of its average net profits during the three immediately preceding financial years would be spent on CSR activities as may be

141. Umakanth Varottil, *Viability of Mandatory CSR*, INDIAN CORP. L. BLOG (Aug. 7, 2010, 2:06 PM), <http://indiakorplaw.blogspot.com/2010/08/viability-of-mandatory-csr.html>.

approved and specified by the company directors.¹⁴² This proposal, which would have been a significant change to Indian corporate law, would have left to the discretion of individual companies, and particularly to the boards of directors, to determine the manner in which the amounts would be deployed.¹⁴³

The proposed mandatory regime for CSR brought many detractors, including many Indian corporate lawyers. These critics noted that a mandatory spend provision was essentially fruitless and would not necessarily render a business socially responsible.¹⁴⁴ For example, given the vagueness in the definition of CSR under the proposed Companies Act, a corporation in a line of business that causes significant detrimental environmental impact could spend the mandatory funds on building a school in a unimpacted rural area rather than on ensuring that it decreased its adverse environmental impact. While this may not be all bad, it certainly falls short of an expansive stakeholder view of CSR. A requirement that companies spend a certain amount of money on CSR activities could potentially lead to greater promoter abuse of corporate funds. Additionally, commentators argued that the MCA's proposal "could provide greater scope for corruption and scams. Worse, this approach will undermine the very concept of CSR and reduce it to provision of lip service in the form of a check-the-box compliance."¹⁴⁵

After much criticism, the MCA announced in late 2010 that it would not make any moves toward mandatory CSR efforts. Instead, the MCA stated that it would regulate CSR through a "comply-or-explain" approach, which requires that firms have a formal CSR policy targeting a 2% spending allocation and to furnish details of funds going to social causes in an annual report.¹⁴⁶ If a company does not have adequate profit or is not in a position to spend the prescribed amount on CSR, the regulation would require the directors to provide disclosure and give suitable reasons in their annual report, with a view to checking non-compliance.¹⁴⁷ The recommendations do not explain in any detail what constitutes CSR.

142. Press Release, Ministry of Corporate Affairs, Recommendation to Make Formulation of a CSR Policy Mandatory for Big Companies (Sept. 10, 2010), available at <http://pib.nic.in/newsite/erelease.aspx?relid=65670>.

143. See Umakanth Varottil, *Movement Towards Mandatory CSR*, INDIAN CORP. L. BLOG (Sep. 11, 2010 11:47 AM), <http://indiacorplaw.blogspot.com/2010/09/movement-towards-mandatory-csr.html>.

144. See Somasekhar Sundaresan, *Govt's approach to CSR gives scope for corruption*, BUS. STANDARD, Sept. 13, 2010, <http://www.business-standard.com/india/news/govt/s-approach-to-csr-gives-scope-for-corruption/407860/>.

145. *Id.*

146. See STANDING COMMITTEE ON FINANCE, *supra* note 54, at 38.

147. *Id.*

This approach has also come under similar criticism with experts asking whether such provisions render CSR a more “check-the-box” obligation and detract from the broader vision of CSR.¹⁴⁸ Commentators have worried whether

the ambiguity on what constitutes spending on CSR, the manner in which the amounts should be deployed and whether corporations can give their mandatory spend[ing] to a trust or foundation run by the business itself can, in fact, lead Indian businesses [to] end[] up spending less than what they currently do on CSR.¹⁴⁹

One important aspect of the CSR Guidelines is the move toward additional disclosure. Very few Indian companies disclose their CSR policies, so additional disclosure could be a tool for NGO advocates and lawyers to work with companies and pressure them to comply with their CSR policies.¹⁵⁰ A recent study of CSR reporting among India’s top 500 companies found that around 49% of these companies were reporting on CSR, but in most reports there is no mention of amount spent.¹⁵¹ Many of these companies “are only making token gestures towards CSR,” working within the philanthropic model rather than the stakeholder model.¹⁵² Another report found that CSR reporting is “qualitative rather than quantitative in nature,” and that most listed Indian companies do not have stand-alone CSR reports.¹⁵³ There is also a larger focus on CSR outputs compared with CSR outcomes.¹⁵⁴ Even for information technology companies, CSR reporting on the Internet is “strikingly low.”¹⁵⁵

Indian firms may not clearly see the benefits of CSR reporting; when asked if there was a business case for CSR reporting, Indian companies were unsure whether the benefits accrued from CSR were from

148. See Satvik Varma, *Legislating CSR*, INDIAN CORP. L. BLOG (Feb. 19, 2011, 5:08 PM), <http://indiakorplaw.blogspot.com/2011/02/legislating-csr.html>.

149. See Satvik Varma, *Coercive Social Responsibility*, ECON. TIMES, Feb. 18, 2011, http://articles.economicstimes.indiatimes.com/2011-02-18/news/28615641_1_csr-social-responsibility-net-profit.

150. See Sharma, *supra* note 96; Lattemann et al., *supra* note 97, at 437. Among Brazil, Russia, India, and China (BRIC countries), Indian firms rank third in CSR communications intensity. Shaomin Li et al., *Corporate Social Responsibility in Emerging Markets*, 50 MGMT. INT’L REV. 635, 646 (2010).

151. Richa Gautam & Anju Singh, *Corporate Social Responsibility Practices in India: A Study of Top 500 Companies*, 2 GLOBAL BUS. MGMT. RES.: AN INT’L J. 41, 49 (2010).

152. *Id.* at 49.

153. C.V. Baxi & Rupamanjari S. Ray, *Corporate Social & Environmental Disclosure & Reporting*, 44(3) INDIAN J. INDUS. REL. 355, 356 (2009).

154. *Id.* at 360.

155. Vidhi Chaudhri & Jian Wang, *Communicating Corporate Social Responsibility on the Internet: A Case Study of the Top 100 Information Technology Companies in India*, 21 MGMT. COMM. Q. 232, 242 (2007).

CSR reporting or actual CSR activities.¹⁵⁶ The respondents were unsure to what extent the role of CSR reporting impacted employee morale, given that the CSR activities were already underway, and they doubted the efficacy of CSR reporting on employees below a certain level of managers.¹⁵⁷ They also did not think CSR reporting improved customer relations because of their already strong reputations.¹⁵⁸ But some companies saw value in CSR reporting, stating that they believed that institutional investors cared about CSR reporting.¹⁵⁹

C. Shortcomings of the Emerging CSR Model

The potential for both corporate governance and corporate social responsibility reforms in India is enormous. There are two important concerns, however, with the Indian government's approach to CSR. First, the mandatory spend provision indicates a more philanthropic model of CSR rather than the broader stakeholder model. Instead of approaching CSR from a holistic viewpoint that addresses the activities of companies in a variety of areas, the government's proposed changes to the Companies Act reduce CSR to a mere 2% spending provision. Second, the government seems to be seeking to capitalize on the cultural values of Indian firms, yet answers the CSR debate with the same solution that it has used with respect to corporate governance reforms—i.e., in large part pinning their hopes on directors.

Both the CSR Guidelines and expected changes to the Companies Act would place the onus on the board of directors to supervise a company's CSR policies and to provide public reports on such policies, including the amount of profits spent on CSR efforts. The problem with placing directors, and invariably independent directors, as central figures is that it could potentially exacerbate the weaknesses in the country's corporate governance model without taking advantage of deep-rooted cultural norms or a broader vision for CSR. The truth is that directors in India still see themselves as strategic advisors to the promoter/founder. Thus, there is a high risk that CSR will not mean a wholesale change in the way a company does business, but will instead remain in the form of programs that emerge out of the founders' desires to create alternatives that challenge existing models or as corporate practices that are shaped by founders' underlying views about social reality and values. Furthermore, given India's primary corporate governance problem (i.e., the domination of promoters and majority stockholders), India's proposed CSR

156. Sulkowski, Parashar & Wei, *supra* note 100, at 805.

157. *Id.* at 803–04.

158. *Id.* at 804.

159. *Id.*

guidelines may exacerbate some of the problems that exist with respect to majority–minority agency costs; controlling stockholders could use the CSR funds on projects that may benefit the promoter at the expense of other shareholders or the company.

CONCLUSION

Since the late 1990s, Indian regulators, as well as Indian industry representatives and companies, have taken significant efforts to overhaul Indian corporate governance. Not only have reform measures been put into place prior to discovery of major corporate governance scandals, but both industry groups and government actors have sprung into action following the Satyam scandal. More recently, regulators have also attempted to address CSR by Indian firms. These efforts, while praiseworthy, fall short of an expansive vision of CSR. Moreover, similar to the corporate governance regime, these efforts place much discretion and power in the hands of board members. The shortcomings discussed in this Article point to the need for reform of the corporate governance norms in India. These shortcomings warn that using the same solution in the CSR realm as the government has used to develop India's corporate governance rules may be misguided.