Akshaya Kamalnath
Work in progress
Please do not circulate without permission

THE HOCUS POCUS OF CORPORATE PURPOSE AND THE VISIBLE HAND OF THE STATE - INSIGHTS FROM INDIA'S CSR EXPERIENCE

Akshaya Kamalnath*

* Lecturer, AUT Law School, akshaya.kamalnath@aut.ac.nz.

Akshaya Kamalnath
Work in progress
Please do not circulate without permission

Abstract

Can corporate law solve the most serious global problems we have? Corporations do have a role to play in issues like climate change, the consequences of using artificial intelligence without adequate safe guards and even inequality. But should corporate law be the vehicle to solve these problems? This article argues that the purpose of the corporation or the 'corporate purpose' is invoked as a kind of hocus pocus to attribute vague responsibilities to corporations. If we allow this kind of hocus pocus to gain ground, we should also be aware that the State will have a dominant say in how corporations are run. Not only will this affect the actual business of the corporation, it will also stifle voluntary programs that corporations might have set up, for the benefit of any set of stakeholders or the society in general. The article studies the mandatory CSR law in India to illustrate this argument. The Indian experiment is useful because it has gone further than most countries in requiring corporations to solve societal problems. The problems it has run into are useful pointers for other countries considering widening or changing corporate law to accommodate a scenario where the corporate purpose must include social goals, as defined by government. The article concludes that the better approach is to incentivize corporations to future-proof themselves against reputational and other damage by incorporating sustainability into its risk metrics.

Table of Contents

1. Introduction

What is the purpose of corporations? Is it to generate wealth for their shareholders or is it to save the world from all its problems? An old cartoon from The New Yorker comes to mind.[1] In it, a man dressed in tattered business attire is sitting around a fire with a group of children telling them that even though the planet got destroyed, "for a beautiful moment in time we created a lot of value for shareholders". The cartoon is apt because it represents a perception that corporations and corporate executives must be blamed for world problems like climate change. Expanding on that, there is a view that since corporations seem to run with the single-minded pursuit of maximising profits, they must be blamed for all problems. Yet, what gets lost in this game of blaming corporations is that it is the responsibility of government to address such problems via environment protection laws and other relevant laws depending on what the problem at hand is.[2]

This article argues that the purpose of the corporation or the 'corporate purpose' is invoked as a kind of hocus pocus to attribute more (and sometimes vaguely defined) responsibility to corporations. If we allow this kind of hocus pocus to gain ground, we should also be aware that the State will acquire a dominant say in how corporations are run. Not only will this affect the actual business of the corporation, but it will also stifle voluntary programs that corporations might have adopted, for the benefit of any set of stakeholders or the society in general. To support this argument, the article uses the example of India, where a mandatory CSR law attempts to enlist corporations in addressing societal problems.

The article is divided into six sections. After introducing the topic in this first section, the second section details recent events that have stirred up the corporate purpose debate. The third section will then examine the concept of corporate purpose and of CSR from a theoretical perspective. Section 4 of the article examines the CSR law in India, its relevance for

[1] Tom Toro, Cartoon Collections (The New Yorker) <https://shop.cartooncollections.com/products/new-yorker-cartoons-tom-toro-cc137952>.
[2] One of the concerns is that big transnational corporations cannot effectively be regulated by individual States. But the solutions thus far have not addressed the issue of transnational corporations. Hence this article will delve into the issue of transnational corporations.

the corporate purpose debate, and its impact. Drawing from the Indian experience section 5 argues against State interference in the business of corporations. Finally, section 6 concludes with some ideas to address social problems without State interference.

2. Recent events stirring up the corporate purpose debate

General incorporation statutes usually do not mention the purpose of corporations. Thus, it is up to each corporation to stipulate its 'purpose' in its constituent documents.[3] Yet, there has been a long-lasting debate about what the corporate purpose should be and, particularly, whether all corporations must have some social purpose.

Milton Friedman, in his controversial 1970 essay said that the 'corporation' has no social responsibilities except to increase its profits.[4] The role of corporate executives, as employees of the owners of the business, was to "conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to their basic rules of the society, both those embodied in law and those embodied in ethical custom".[5] Since Friedman's essay was published, there has been no dearth of criticism of the ideas in it. Most of the criticism focuses on the part of the article that decries the idea of social responsibility of corporations.

Fast-forwarding to 2018 and 2019, several events have put the corporate purpose debate back on the table. The first event was the proposal in 2018 in the U.S., of a bill entitled 'the Accountable Capitalism Act' by presidential hopeful Senator Elizabeth Warren.[6] The proposal would require large companies (those generating a revenue of over $1 billion) to apply for a federal charter which would then tell company boards to consider the interests of all

[3] This is one of the aspects central to the corporate form. See Miller, Paul B and Gold, Andrew S, 'The Corporation as a Category in Private Law' in Hanoch Dagan and Benjamin Zipursky, (eds), *Research Handbook on Private Law Theories* (Elgar, forthcoming) available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3453744> 8 – 11. Prior to the introduction of general incorporation statutes, the King chartered corporations for specific purposes and these purposes usually had a 'public' or 'social' element. See Robert C Hockett, 'When all Enterprise was Social' 89 in Benjamin Means and Joseph W. Yockey, (Eds) The Cambridge Handbook of Social Enterprise Law (CUP, 2018).

[4] Milton Friedman, 'The Social Responsibility of Business is to Increase its Profits' *New York Times* (New York, 13 September 1970) available at <https://www.bnicapital.ch/files/friedman.pdf>.

[5] Ibid.

[6] Accountable Capitalism Act (2018) <https://www.warren.senate.gov/imo/media/doc/Accountable%20Capitalism%20Act%20One-Pager.pdf>

stakeholders and not only those of shareholders.[7] The rationale was that corporations should be expected to act as good citizens in exchange for the corporate personality granted to them. Thus, this proposal goes beyond Friedman's expectation that corporate executives conduct business in accordance of the interests of owners. Instead, it allows the State, in effect, to tell company boards (and the executives on these boards) how to conduct their business.

This was followed up in early 2019, by the annual letter from Larry Fink, the head of Blackrock Inc., one of the largest fund management firms, addressed to the CEOs of companies in which Blackrock invests.[8] After describing current global problems like stagnant wages, excessive nationalism, the danger of losing jobs to technology etc, Fink asks CEOs to move away from the pursuit of short-term shareholder returns and run their businesses with a 'purpose'. This purpose, according to Fink, should be what drives businesses to create value for stakeholders other than shareholders. For instance, he says:

"*…companies must embrace a greater responsibility to help workers navigate retirement, lending their expertise and capacity for innovation to solve this immense global challenge. In doing so, companies will create not just a more stable and engaged workforce, but also a more economically secure population in the places where they operate.*"

While it seems like Fink is also going beyond Friedman's idea of profit maximisation and advocating a role for corporations in solving world problems, one could argue that Fink's letter is steeped in the idea of ensuring long term shareholder value. By saying that assuring workers of security post-retirement, corporations will be able to ensure that their workforce is more engaged today, Fink is simply suggesting ways of enhancing shareholder value in the long term. As Fink puts it, "purpose guides culture, provides a framework for consistent decision-making, and, ultimately, helps sustain long-term financial returns for the shareholders of your company".[9] Yet Fink couches the need for a focus on long term shareholder value in terms of corporations addressing "pressing social and economic issues" because of the "failure of government to provide lasting solutions" to these issues.[10] However, he stops short of explicitly inviting the State to make regulations in this regard.

[7] Id.
[8] Larry Fink, 'Purpose & Profit' available at <https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter>
[9] Ibid.
[10] Ibid.

On the heels of Warren's proposal and Fink's letter, came the 2019 statement by the Business Roundtable on corporate purpose. The Business Roundtable consists of nearly 200 CEOs of Americas largest corporations.[11] Although the statement begins by reinforcing a belief in the free market system, it goes on to make 'a fundamental commitment to all stakeholders'.[12] This commitment to stakeholders is elaborated on by stressing a commitment to customers, employees, suppliers, communities, and finally, 'long-term value' for shareholders.[13] In other words, this too can simply be explained as a commitment to all stakeholders inasmuch as it furthers the goal of enhancing shareholder value in the long term. However, if the intention were simply to express a commitment to long-term shareholder value the statement would not begin with a comment about Americans deserving "an economy that allows each person to succeed through hard work and creativity and to lead a life of meaning and dignity". While the State may be charged with ensuring people's right to a life of dignity and meaning, corporations surely cannot not be charged with this responsibility? Even if this is empty rhetoric as some have suggested[14], such a statement might act as an invitation for State regulation.

An invitation for government regulation to requiring companies to solve world problems leads us to an expectation that corporations are a collective Atlas holding up the world even where government fails. If, indeed, we are set to make this turn in regulating corporations, it would be a mistaken turn and one that would be hugely costly. It is a mistaken turn because corporations already contribute to society by wealth generation since, in the process of generating wealth for shareholders, they provide jobs to employees and business to contractors and they also efficiently produce useful products and services for consumers. By requiring them to take on the role of government, not only would their business become less efficient, but in addition to this would allow government a free pass for failing in their own purpose.

Besides, if corporations are charged with solving societal problems, this amounts to endowing such public powers in corporate executives, who were not elected by citizens.[15] Further,

[11] The Business Roundtable Statement, 'Statement on the Purpose of a Corporation' <https://opportunity.businessroundtable.org/wp-content/uploads/2019/09/BRT-Statement-on-the-Purpose-of-a-Corporation-with-Signatures.pdf>.
[12] Ibid.
[13] Ibid.
[14] Andrew Winston, 'Is the Business Roundtable Statement Just Empty Rhetoric?' *Harvard Business Review* (30 August 2019) <https://hbr.org/2019/08/is-the-business-roundtable-statement-just-empty-rhetoric>.
[15] See Milton Friedman, (n 4).

requiring corporations to solve societal problems would run into the classic 'many masters' problem, where directors who are answerable to many masters (shareholders and other stakeholders) would in effect be accountable to none.[16] Finally, such requirements would stymie any innovative and voluntary efforts of corporations that may be motivated by the reputational benefits of such efforts. This is because, in a world where acting for social good or social responsibility is necessary, all corporations would engage in the bare minimum of such activities since voluntary efforts will not stand out any longer.

Before addressing these arguments in greater detail, it is useful to engage in a discussion of corporate theories. After all, the 'corporate purpose' debate is not new. What is new or what makes the issue more urgent at this point is that the costs of taking a wrong turn would be drastic, since the world is now faced with new challenges alongside old ones. Climate change is a real threat, thus making the scene in The New Yorker cartoon not too far-fetched. Another issue is that of the impact of using artificial intelligence in various fields.[17] These problems need answers and while corporations should be part of any solutions we come up with, they cannot be charged with tasks that they are ill-equipped to undertake.

3. Corporate purpose and CSR

The question of what the purpose of the corporation should be has been answered differently at different times. For the most part, our understanding of the nature of the corporation has tended to oscillate between two views, namely the property conception of the corporation on the one hand and the social entity conception on the other.[18] While the former puts shareholders at the forefront, the latter puts shareholders on a par with other stakeholders.

The social entity conception or concession theory viewed the corporation as existing separately from its shareholders. This view was the dominant view of the corporation in the early nineteenth century.[19] The justification for this view can be found in the context of states having

[16] Frank H. Easterbrook & Daniel R. Fischel, *The Economic Structure of Corporate Law* (HUP, 1991) 38.
[17] Larry Fink's letter mentions the effect of technology on jobs but this is just one facet. Another example is where the use of AI might impact privacy of consumers and so corporations might have to consider the interests of consumers.
[18] William T Allen, 'Our Schizophrenic Conception of the Business Corporation' (1992) 14 Cardozo L Rev 261, 264.
[19] David Millon, 'Theories of the Corporation' (1990) 1990 Duke LJ 201, 205 - 206.

to legislate a special statute for each incorporation. Thus, since the government statute facilitated the incorporation, this view understands the corporate purpose as inclusive of the general welfare.[20] In other words, the corporation's purpose would not only extend to the interests of the shareholders but also to all those interested in or affected by the corporation.[21] This is also known as the stakeholder model of the corporation.

The property conception understands the corporation as the private property of its shareholders. Under this view, the sole purpose of the corporation is to maximise the wealth of its shareholders.[22] Since it gives primary importance to the shareholders, it is also called the shareholder primacy model.[23] Deviating slightly from the focus on the property conception of the corporation, contemporary scholars view the corporation as a 'nexus of contracts' consisting of various stakeholders in the corporate enterprise including shareholders, consumers, employees and creditors. Although the nexus of contracts view does not consider the corporation as the property of shareholders, it still subscribes to the shareholder primacy model. This is because shareholder primacy is the contractual term that all constituencies would agree to if they had actually negotiated with each other.[24]

The debate over the shareholder primacy model versus the stakeholder model is also reflected in the famous exchange between Berle and Dodd in 1968. Berle opined that the powers of the corporation or the management of the corporation are 'at all times exercisable only for the ratable benefit of all the shareholders as their interest appears'.[25] Dodd responded that corporations not only have a profit-making function but also a social service function and, therefore, their purpose was more than just to make money for its shareholders and included securing the welfare of employees, consumers and the community as a whole.[26] Although Dodd did not use the term, he advocated, in effect, for a stakeholder model. However, as he himself clarified, Dodd's view of designating a 'social responsibility' for businesses was 'merely a more enlightened view as to the ultimate advantage of the stockholder-owners' and thus did not

[20] Allen, (n 18), 265.
[21] Id.
[22] A A Jr Berle, 'Corporate Powers As Powers in Trust' (1931) 44 Harv L Rev 1049 - 1074.
[23] Allen, (n 10), 265.
[24] Stephen M. Bainbridge, *The New Corporate Governance in Theory and Practice* (OUP, 2008), 28 - 30.
[25] Berle, (n 22), 1049-1074.
[26] E Merrick Jr Dodd, 'For Whom are Corporate Managers Trustees' (1932) 45 Harv L Rev 1145, 1148.

require a departure from the traditional goal of shareholder wealth maximization.[27] This enlightened view of shareholder value is often called long-term shareholder value because the management of stakeholder interests is ultimately in the interests of shareholders in the long-term even if it results in reduced profits in the short-term.

This view of shareholder value is the underlying principle in corporate law in most jurisdictions and the long-term shareholder value idea has gained acceptance in most jurisdictions. Even in Delaware, directors have the discretion to consider and further the interests of non-shareholder stakeholders.[28] In the UK, the long - term shareholder value meaning of corporate purpose was codified in the Companies Act 2006 by means of s172.[29] It introduced what is known as the enlightened shareholder value (ESV) model. Ultimately, even under this model, discretion has been given to directors to decide the course of action that is likely to promote the success of the company. However, the legislature provides guidance in determining what the 'success of the company' means. It provides that directors should promote the success of the company for the benefit of its members as a whole, and that directors should also have regard to the following factors: the long-term consequences of board decisions; interests of employees; the company's business relationships (with suppliers, customers and others); the impact of the company's operations on the community and the environment; the company's reputation; and fairness between members of the company.[30] Ultimately it is up to corporate managers to decide whether or not to engage in activities that can be attributed to a social purpose or a purpose relating to the welfare of non-shareholder groups. Thus, the interests of shareholders are still prioritized over that of other stakeholders. Some scholars have therefore opined that the introduction of the ESV model in s 172 ultimately did not change the corporate purpose.[31]

---

[27] Ibid 1156.

[28] See Peter A. Atkins, Marc S. Gerber, and Edward B. Micheletti, 'Putting to Rest the Debate Between CSR and Current Corporate Law' *Harvard Law School Forum on Corporate Governance and Financial Regulation* (7 September 2019) <https://corpgov.law.harvard.edu/2019/09/07/putting-to-rest-the-debate-between-csr-and-current-corporate-law/>. See also Joan MacLeod Heminway, 'Let's Not Give up on Traditional For-Profit Corporations for Sustainable Social Enterprise' (2018) 86 UMKC L Rev 779 arguing that sustainable social enterprises can and are being run as traditional for-profit corporations

[29] U.K. Companies Act, 2006, s 172

[30] U.K. Companies Act, 2006, s 172(1)

[31] Bernali Choudhury and Martin Petrin 'Corporate governance that 'works for everyone': promoting public policies through corporate governance mechanisms' (2018) 18 (2) J. Corp. L. Stud. 381, 387. Choudhury and Petrin go on to say that in so prioritising shareholder interests, UK law has gone beyond US law which remains agnostic about interpreting the corporate purpose.

However, the idea of corporations having a social responsibility beyond business purpose (or corporate social responsibility as it has become popularly known) never died down. In fact, calls for corporations to become socially responsible grew louder over time. Berger-Walliser and Scott note that from 1986 to 1996, only 140 American law review articles mentioned 'corporate social responsibility' (CSR), while from 1996 to 2006, 717 American law review articles mentioned it and the number more than doubled to 2138 from 2006 to 2016.[32] In 2013 the American Bar Association's Business Law Section created a subcommittee on Corporate Social Responsibility Law.[33]

Despite the rising popularity of the idea of CSR, there was and still is no universally accepted definition of CSR.[34] As Robinson observed, the "phrase has proven remarkably resistant to definitive ethical analysis or practical application".[35] Because of this confusion, some scholars have preferred not to use the term CSR.[36] Going back to Friedman, the social responsibility of the firm is to increase its profits.[37] Obviously, most users do not mean a corporation's pursuit of profits when using the term CSR. In legal scholarship, CSR has come to mean a corporation's responsibility towards stakeholders like employees, local communities, creditors, consumers and the environment.[38] Management literature often cites the definition by Bowen, i.e. the obligations of business people to pursue those policies, to make those decisions or to follow those lines of action which are desirable in terms of the objectives and values of society.[39]

---

[32] Gerlinde Berger-Walliser and Inara Scott, "Redefining Corporate Social Responsibility in an Era of Globalization and Regulatory Hardening" (2018) 55 (1) Am. Bus. L.J. 167, 168.
[33] Ibid.
[34] Crane et. al., 'The Corporate Social Responsibility Agenda' 5 in Crane et. al (eds.) *The Oxford Handbook of Corporate Social Responsibility* (OUP, 2008).
[35] John H Robinson, 'Corporate Social Responsibility' (1987) 2 Notre Dame JL Ethics & Pub Pol'y 733.
[36] See eg., Beate Sjåfjell & Linn Anker Sørensen, "The Duties of the Board and Corporate Social Responsibility (CSR)" 4, 5 in Hanne Birkmose, Mette Neville & Karsten Engsig Sørensen (eds.), *Boards of Directors in European Companies – Reshaping and Harmonising their Organisation and Duties* (Kluwer Law International, 2013).
[37] Friedman, (n. 15).
[38] See eg., Afra Afsharipour and Shruti Rana, 'The Emergence of New Corporate Social Responsibility Regimes in China and India' (2013) 14 UC Davis Bus LJ 175, 186. See also Constance Z Wagner, 'Evolving Norms of Corporate Social Responsibility: Lessons Learned from the European Union Directive on Non-Financial Reporting' (2018) 19 Transactions: Tenn J Bus L 619, 621. Wagner defines CSR as the 'notion that corporations are accountable for their social and environmental impacts'.
[39] Archie B. Carroll, 'A History of Corporate Social Responsibility' in Crane et. al. (Eds.) (n. 34).

In terms of the practical application of CSR, Murphy has outlined four phases of CSR. CSR before the 1950s was philanthropic and consisted of donations to charities either by corporations or corporate executives personally.[40] From the early 1950s to the late 1960s, there was a rise in overall awareness about the responsibility of business and then from the late 1960s to the early 1970s companies began to focus on specific issues like pollution, race discrimination, etc. From the mid-1970s onwards was the fourth phase when companies began to take actions along the lines of examining corporate ethics and using social performance disclosures. Thus, the fourth phase could be seen to coalesce with the legal understanding of companies conducting operations ethically i.e. with regard to the impact of such operations on various stakeholders. Disclosure of such social performance, or non-financial information as it is more commonly called, has today been integrated into the corporate law and regulatory codes of many jurisdictions.

From a theoretical perspective, the justifications for why corporations engaged in CSR either followed the long-term shareholder value argument or the stakeholder interests argument. While the former is easy to rationalize under the existing legal framework, the latter argument is a more difficult fit. When corporations say that serving stakeholders or society in general is the right thing to do, we run into Friedman's worries about whether this is in line with the interests and desires of the owners i.e. the shareholders.

Chaffee has proposed a theory that helps justify the latter argument for engaging in CSR i.e. the stakeholder interests argument. According to his theory CSR is justified because it is the right thing to do or the socially desirable thing to do. Pointing out that many existing theories focus on how the corporation exists rather than why the corporation exists, he proposes the collaboration theory that tries to answer both questions of corporate existence and corporate purpose.[41] According to this theory, corporations are collaborations among the government and the people who organize, operate, and own them. The corporation owes its existence to this collaboration.[42] Under this theory, CSR is justified not only on the basis of the corporation owing its existence to the State but also because 'the contractual nature of a corporation creates

[40] Ibid citing Patrick Murphy, 'An Evolution: Corporate Social Responsibility' (1978) University of Michigan Business Review. A famous (or infamous) example is that of Elihu Yale, governor of the East India Company donating £ 500 to a college in Connecticut which later became Yale College.
[41] Eric C Chaffee, 'The Origins of Corporate Social Responsibility' (2017) 85 U Cin L Rev 353, 370.
[42] Ibid, 370

a fiduciary duty of good faith among the collaborating parties to treat each other well within the terms of the deal that they have struck in regard to creation and operation of the business'.[43]

Ultimately, Chaffee's theory conceives of CSR as something for-profit corporations should engage in, in three situations. The first situation is when there is a happy meeting of both profit maximization and social motives.[44] The second situation is where it does not cost the company anything to engage in CSR i.e. the CSR activity is cost-neutral. The third situation is where the financial implications of the CSR activity is uncertain.[45] While the first situation does not seem to be at odds with the long-term shareholder view up to this point, the remaining two situations require corporations to engage in CSR even where it is unclear whether the action would support profit maximization. The reason collaboration theory stipulates that corporations should engage in CSR even in the second and third situation is that those organizing, operating, and owning corporations have agreed to treat the State well when they agreed to collaborate with the State. Because the government represents the will of the people in a democracy, the idea of treating the State well is to be interpreted as treating society in a way that supports its well-being.[46] Thus, CSR goes beyond the enlightened shareholder value or long-term shareholder value models which only allows corporations to engage in CSR when it benefits the shareholders either immediately or in the long term. Although distinct from the concession theory, the collaboration theory also allows a big role for the State in the existence of the corporation. Yet, it stops short of holding corporations responsible for solving societal problems, especially where there are negative costs for shareholders.

Sjåfjell and Sørensen propose an understanding of CSR that goes even beyond the collaboration theory. Their rationale for CSR is articulated from the perspective of sustainability. They outline three essential features of CSR, for it to credibly ensure that companies can play a role in addressing issues of sustainability.[47] The first feature is that the promotion of CSR should encompass both the level of compliance and action beyond compliance.[48] In other words, even if the law requires some form of CSR, this should not

[43] Ibid.
[44] Ibid, 369.
[45] Ibid, 370.
[46] Ibid, 369.
[47] Beate Sjåfjell and Linn Anker Sørensen, (n. 36) 5.
[48] Ibid, 6.

exclude voluntary CSR activities by companies. The second feature is that CSR must be integrated into the conduct of the company's business and its impacts.[49] Third, and somewhat related to the second feature, is that CSR must integrate environmental and social concerns in the decision-making of the company in such a way as to lead to an internalisation of externalities.[50] Under this model, the non-voluntary CSR expectation from companies is that they are only responsible for the problems created by their own conduct.

Thus, under this model, the rationale for CSR is that corporations must internalise the costs of their business conduct when such conduct is responsible for problems like climate change, human rights violations, etc. These costs are currently borne by other stakeholders, for instance the victims of human rights violations or the victims of environmental pollution caused by companies. However, this model does not require companies to solve other societal problems unrelated to its business.

It is clear from the above discussion that although CSR started out as a voluntary concept or something corporate executives could engage in at their discretion, the expectation that corporations engage in CSR is beginning to take on a mandatory flavor. Berger-Walliser and Scott find in their study that CSR has become subject to government regulation in many countries.[51] The push from politicians, the Business Roundtable and influential figures like Larry Fink, alongside academic scholarship in this regard, suggests that government regulation requiring CSR or some form of stakeholder centric approach by corporations is probable in the US. It is therefore useful to examine how government regulation has worked in India in this regard.

4. India's CSR law

CSR was voluntary in India up until 2013 when the country's company law was revamped via the Companies Act, 2013.[52] The 2013 law introduced a CSR provision, section 135, which

[49] Ibid.
[50] Id.
[51] Berger-Walliser and Scott, (n. 32). China, India and Indonesia are examples of jurisdictions where CSR has been subject to government regulation.
[52] The Companies Act, 2013 (India), No. 18, Acts of Parliament, 2013.

required large[53] companies to annually spend at least two percent of their average net profits generated in the preceding three financial years on CSR activities.[54]

The Companies Act also specified what would be considered as a CSR activity.[55] Two of these categories deal with healthcare.[56] Another two of the categories deal with education.[57] The other categories are: promoting gender equality and empowering women; ensuring environmental sustainability; and contribution to government funds. There is also an opening for the government to specify other categories of activities to be considered as CSR activities. Clearly, these categories are areas which would normally be within the government's mandate. Tellingly, the government's justification for the CSR provision speaks of corporations taking on some government responsibilities:

> [Corporations] owe it to the people and the society to pay them back in terms of social services and by building social capital for common good. This cannot be the sole responsibility of governments.[58]

Further emphasizing the nature of CSR under the law, the Companies (Corporate Social Responsibility Policy) Rules notified in 2014 stated that only activities specified in the Companies Act, 2013 would be considered as CSR.[59] In other words, the generally understood idea of CSR i.e. a corporation conducting its business in a socially responsible manner would not be assumed to be CSR under the law in India. Thus, any corporation in India choosing to follow the guiding principles of Chaffee's collaboration theory, would also have to spend the required percentage of its profits on the categories specified by the government. Similarly, corporations that follow the CSR model outlined by Sjåfjell and Sørensen and try to internalise the costs of their business conduct (rather than pass them on to other stakeholders) by engaging in sustainable business practices would still have to spend additional funds to comply with the Indian CSR law.

---

[53] The section applies to companies that have a net worth of at least rupees 500 crore (approximately eighty million US dollars) or those that have an annual turnover of at least rupees 1,000 crore (approximately eight hundred thousand US dollars.

[54] The Companies Act, 2013 (India), Section 135(5).

[55] The Companies Act 2013 (India), Schedule VII.

[56] They are worded as 'reducing child mortality and improving maternal health'; and 'combating human immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases'.

[57] They are worded as the promotion of education; and employment enhancing vocational skills.

[58] Ministry of Corporate Affairs, Standing Comm. on Fin., Companies Bill, 2011, Fifty-Seventh Rep. 99 (2011-2012) at 106.

[59] Companies (Corporate Social Responsibility Policy) Rules (India), 2014.

Thus, India's CSR law harks back to the early CSR phase (as per the four phases outlined by Murphy) which mainly consisted of philanthropy except that it makes such philanthropy mandatory. It also harks back to a later phase when corporations chose to address certain problems like pollution or race discrimination, but, again, the government has a specific list of activities to be undertaken and thus decides on the problems that need to be addressed.[60]

Although corporations that voluntarily undertake to solve societal problems do so because the government has not or for some reason has been unable to step in, by making CSR a mandatory requirement, there is a sense that government has passed on some of its inherent duties to corporations. Nevertheless, there is room to view the law as a nudge encouraging corporations to engage in the public good since the enforcement of CSR is largely left to shareholders. The only requirement is for the board of directors to disclose the details of the CSR budget spent in their annual report and on the company's website; and if they have not complied with the requirements of s135, they have to explain the reasons for it.[61] Thus, it left it to shareholders to question management about the level of compliance with the CSR provision. However, the alternate view that the CSR requirement is mandatory in nature is also plausible because section 135 also imposed a duty on the board of directors to spend the requisite amount on CSR activities, albeit with some wiggle room for non-compliance.[62] Indeed, many commentators take the view that the provision was mandatory in nature.[63] Varottil describes India's CSR model as a quasi-mandatory or hybrid approach because companies are required to spend the requisite amount on CSR but also have the flexibility to explain and justify if they do not do so.[64] Thus, while there is flexibility with regard to the expenditure on CSR, disclosure is mandatory.[65]

---

[60] For a discussion on how much flexibility there is for companies to interpret the list of activities provided see Sandeep Gopalan and Akshaya Kamalnath, 'Mandatory Corporate Social Responsibility as a Vehicle for Reducing Inequality: An Indian Solution for Piketty and the Millennials' (2015) 10 Nw J L & Soc Pol'y 34

[61] The Companies Act, Section 135(5).

[62] The Companies Act, Section 135(5).

[63] See eg., Dhammika Dharmapala and Vikramaditya S. Khanna, 'The Impact of Mandated Corporate Social Responsibility: Evidence from India's Companies Act of 2013' (2018) 56 International Review of Law and Economics 92-104.

[64] Umakanth Varottil, 'Analysing the CSR Spending Requirements under Indian Company Law' in Jean J. du Plessis, Umakanth Varottil & Jeroen Veldman (eds.), *Globalisation of Corporate Social Responsibility and its Impact on Corporate Governance* (Switzerland: Springer International Publishing, 2018).

[65] Ibid.

4.1 What is the 'corporate purpose' in India?

The law that introduced the CSR provision also introduced an amendment to the provision dealing with the duties of directors. Section 166 of the Companies Act, 2013 codified the duties of directors, and states in relevant part, as follows[66]:

> A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.

Thus, the section seems to draw inspiration from the UKs Enlightened Shareholder Value model with directors being required, in acting in the interests of the company, to consider not only the interests of shareholders but also that of stakeholders such as employees, the community and the environment. However, unlike in the UK, where shareholders must be prioritised above the interests of other stakeholders, the Indian provision seems to put the interests of all stakeholders (including shareholders) on equal footing.[67] If the interests of all stakeholders must be considered in this way, we run into the problem of how conflicting interests of various stakeholders should be balanced and neither the Companies Act, 2013 nor other regulations provide any guidance of how these conflicts should be resolved.[68] Thus, even though the corporate purpose has been widened, it might not have much impact in practice because of the lack of clarity.

Afsharipour points out that since CSR has been worded as a board function, it cannot be separated from the company's corporate governance.[69] However, since the content of the CSR duty clearly focuses on philanthropy rather than on responsible business practices, it seems to

---

[66] Section 166(2) of the Companies Act, 2013 (India).

[67] See Afra Afsharipour, 'Redefining Corporate Purpose: An International Perspective' (2017) 40 Seattle U L Rev 465, 490.

[68] Khanna and Varottil, 'Board independence in India: From form to function?' (2017), in Dan W. Puchniak, Harald Baum and Luke Nottage (eds.), *Independent Directors in Asia: A Historical, Contextual and Comparative Approach* (Cambridge: Cambridge University Press, 2017) available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2752401> pp. 26–27.

[69] Afra Afsharipour, 'Corporate Social Responsibility and the Corporate Board: Assessing the Indian Experiment' in Jean J. du Plessis, Umakanth Varottil & Jeroen Veldman (eds.), *Globalisation of Corporate Social Responsibility and its Impact on Corporate Governance* (Switzerland: Springer International Publishing, 2018) available online at < https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3355808> 12.

be rather a fringe duty that the board must comply with (or not if they give reasons for non-compliance), rather an integral part of governance. It is still possible to take the view that Section 166 encourages the company to conduct its business in a socially responsible way, thus incorporating the more commonly accepted idea of CSR. Even if this is the case, unless there is more guidance, section 166 would merely be a nod to the idea of long-term shareholder value.

4.2 Impact of the CSR law on companies

Ultimately, the Indian CSR provision was a novel experiment in two ways. For one thing, it converted a voluntary concept into a mandatory requirement (through a comply or explain mechanism). For another thing, it focused on philanthropic spending in government specified areas rather than on the conduct of business operations in a manner that considers the interests of their various stakeholders. Although the reaction of the business community was initially negative[70], many of the largest companies eventually took it in their stride. A 2015 analysis found that 44 of the top 50 companies listed on the National Stock Exchange of India had a CSR page on their website which expressed the government's view of CSR i.e. focused on nation building and philanthropy.[71] Only a small number of the fifty companies rationalised CSR as a reputation enhancing tool to ultimately increase long term shareholder value.[72] However, the study also reports that some companies included the use of sustainable technologies and affirmative action in employment policies as part of their CSR strategy.[73] Clearly, some companies consider the conduct of business in socially responsible ways as CSR, despite the attempt to change the meaning via section 135.

A 2016 study by Dharmapala and Khanna throws more light on the impact of the CSR provision. It found, based on a sample of 55 of the top 100 companies, that 10 firms had met or even exceeded the 2% CSR expenditure required, even before section 135 came into effect. These firms, according to the study, reduced their CSR spending after the new law was

[70] Akhila Vijayaraghavan, 'Indian Industries Oppose Mandatory CSR Reporting', *Just Means*, (August 16, 2010)
available at: <http://www.justmeans.com/editorials?action=readeditorial&p=26759>.
[71] Sandeep Gopalan and Akshaya Kamalnath, (n 60), 81.
[72] Ibid, 81, 84.
[73] Ibid, 85.

introduced. The other 45 firms were spending less than 2% on CSR prior to section 135's coming into effect but increased their spending after that time. However, on balance, the overall CSR spending increased among the 55 firms in the sample. Further, not all companies complied. The study found that even larger companies chose to explain non-compliance rather than to spend the 2% as required.[74] Another study by Varottil found that 45% of the Nifty 100 companies were not compliant with the law in the 2015-2016 financial year (i.e. the second year of the law's operation).[75] Varottil also notes that companies that failed to comply simply engaged in boilerplate disclosures or failed to make any disclosure at all.[76] Another interesting finding from the study by Dharmapala and Khanna is that firms with advertising expenses substituted the advertising spending with CSR spending.[77]

Taken together, these findings tell a story about whether corporate executives genuinely believe in CSR, and, in particular, the way in which section 135 defines it. Although many companies may have echoed the government's rationale for CSR on their webpage, not all of them fully agree with the rationale of, or need for CSR. This is most likely why some companies choose to publicise responsible business conduct as CSR, even though the law does not include it in its CSR definition and also why other companies have chosen not to comply with the law. The substitution of advertising expenses with the required CSR spending is in line with other studies that show that the motivation to engage in CSR can largely be attributed to its reputational benefits.[78] Further, the law imposing a standard CSR spending requirement for all companies of a certain size might have had the impact of reducing the reputational benefits of CSR. In other words, the spending now becomes the fulfilment of a legal requirement rather than something voluntary that can help the company stand out from its peers. This is likely why those companies that were engaging in philanthropic spending beyond 2% seem to have reduced such spending to the level now mandated by the law. Further, the finding that companies that did not comply with the CSR spending requirement engaged in boilerplate explanations for such non-spending suggests that they do not expect their shareholders to be interested in such CSR spending.

[74] Dharmapala and Khanna, (n 63).
[75] Umakanth Varottil, (n. 64),16.
[76] Ibid, 17.
[77] Dharmapala and Khanna, (n 63).
[78] See Zhichuan Frank Li, Taylor Morris and Brian Young, "Corporate Visibility in Print Media and Corporate Social Responsibility" available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3394956>.

In respect of the question whether the CSR spending had made an impact in terms of solving the social problems in the country, it was found that the least developed states within India had received only 9% of the CSR spending while states with low poverty levels received about 40% of the CSR spending.[79] Of course this could simply be attributed to the fact that companies would rather spend their CSR amount on areas and communities around where they themselves are located to be able to harness any reputational benefits of CSR.[80] However, this data, when assessed against the government's rationale of requiring that corporations undertake responsibility, along with the government, to build 'social capital for common good' shows that the CSR provision is not the most effective way to build social capital for the betterment of the common good in the entire country.

4.3 Attempted amendments to the CSR law

A recent amendment to the 2013 CSR provision added penalties including imprisonment for officers of companies that do not comply with the provision.[81] These changes were initially put 'on hold' and later scrapped in response to protests from the business community.[82] As a first step, the amendment had proposed that any unspent CSR amount that was committed to ongoing projects would be transferred into an escrow account for three financial years. If the amount remained unspent after the three years, then it would have to be moved into government funds like the Prime Minister's Relief Fund. Failure to comply with these requirements could result in monetary penalties not only for the company, but also for every officer of the company.[83] Additionally, every company officer could also be subjected to imprisonment of up to three years.[84]

---

[79] Gireesh Chandra Prasad, 'Who gains the most from corporate charity?' *Live Mint* (23 August 2019) available at <https://www.livemint.com/companies/news/who-gains-the-most-from-corporate-charity-1566536241870.html>.
[80] Ibid.
[81] The Companies Amendment Bill 2019 (India) (Bill No. 189 of 2019) <http://www.prsindia.org/sites/default/files/bill_files/Companies%20%28Amendment%29%20Bill%2C%202019_0.pdf>.
[82] K R Srivats, 'Ministry keeps new CSR amendments on hold' *The Hindu Business Line* (18 August 2019) <https://www.thehindubusinessline.com/economy/policy/ministry-keeps-new-csr-amendments-in-abeyance/article29127073.ece>.
[83] Varottil, (n 81).
[84] Ibid.

It is unsurprising that the amendment provoked considerable criticism. Business executives were worried that the penalties were too harsh and could lead to harassment of companies by government officials.[85] Conceptually, the amendment would have changed the understanding of CSR from enforced philanthropy with the goal of addressing societal problems to that of enforced contributions to the government. Under the current provision, even if the amount to be spent and broad areas to spend it in are provided by government, there is still some flexibility for companies to be able to create programs that also enhance their reputation. However, had the amendment been introduced, companies may have preferred to simply treat the CSR expenditure as if it were a tax and transfer the money to government funds directly rather than risk commencing projects that might not fully consume the allocated amount in the given time period.

Conceptually, the proposed amendment would have further divorced CSR from the corporate purpose i.e. promoting long term shareholder value. Instead of expenditure on issues beneficial to the company's stakeholders, if most corporations decided that the safest route was to give the required amount to government, stakeholders would lose out on any innovative CSR programs that individual corporations might have designed. Clearly, mandatory CSR requirements with this kind of teeth risk killing voluntary initiatives of companies for the welfare of any of their stakeholders.

This failed attempt by the government, to further interfere in CSR should be taken as a warning by other jurisdictions where Sate interference is being proposed. Ultimately, it is preferable that the corporate purpose should be understood as something for the board of each company to decide upon.

5. The visible hand of the State

The theoretical discussion in section 3 of this article shows that invoking the expansion of corporate purpose beyond shareholder wealth maximisation is often fraught with uncertainty in

[85] Vatsala Gaur and Maulik Vyas, 'Jail term for CSR violation makes firms anxious' *The Economic Times* (3 August 2019) <https://economictimes.indiatimes.com/news/company/corporate-trends/jail-term-for-csr-violation-makes-firms-anxious/articleshow/70506775.cms>

terms of pursuing a balance in respect of the various stakeholder interests. Because of this uncertainty, arguments for a move away from shareholder wealth maximisation often sound like hocus pocus. Thus, the status quo has not changed except to allow directors the express discretion to consider interests of stakeholders when such focus is in the long-term interests of shareholders. The CSR provision in India has revealed that requiring corporations to undertake public functions of addressing societal problems is not efficient for a number of reasons.

First, the government is better positioned to address these problems not only because individual companies do not have the breadth or societal penetration of a government but also because a corporation's incentives are obviously different from that of government.[86] Even corporations that have been voluntarily engaging in philanthropic activities are motivated by pet projects and issues and/ or the considered benefits of such projects to their corporation. Secondly, and related to incentives, when CSR becomes mandatorily imposed by the State, the reputational gains associated with such CSR-related actions will be lost and hence will likely act as a disincentive to engaging in CSR beyond what is minimally required by law. Thirdly, the State can merely require corporations to undertake some actions for the public good or spend certain amount of money as has been done in India; but will not be able to provide effective guidance to corporate boards in terms of resolving conflicts between the various stakeholders. The 'many masters' problem, where directors who are accountable to all stakeholders will in effect be accountable to none and hence might engage in self-interested activities, is very real. Even if we want corporations to internalise the costs of any externalities, it would be hard to achieve that by widening the corporate purpose and hence requiring directors to owe duties to all stakeholders. As Bainbridge argued in 1993, "unless managers are to be held strictly liable for decisions that harm some nonshareholder constituency, hindsight cannot be used when measuring their compliance with their multi-fiduciary responsibility".[87]

Neither Larry Fink nor the Business Roundtable have found a way to solve the 'many masters' problem and have ultimately fallen back on the idea of addressing societal problems because it is, in effect, in the long-term interest of the shareholders. Even Senator Warren's proposal only

[86] 'Mandating CSR spending won't help' *Business Standard* (January 10, 2016) <https://www.business-standard.com/article/opinion/csr-reality-checks-116011000640_1.html>.
[87] Stephen M. Bainbridge, 'In Defense of the Shareholder Wealth Maximization Norm' (1993) 50 Washington & Lee Law Review 1423.

states that large companies would be required to consider the interests of all stakeholders but does not explain how these interests should be prioritised. However, because the underlying motives of her proposal are similar to those of the government in India, it is likely that her model would require corporations to engage in solving inequality and other problems as the government directs. With such intervention, large corporations will have to contend with the visible hand of the State in that they would have to do the State's bidding. This would put corporations in the difficult position of attempting to run their business efficiently while at the same time having to take on some of the State's responsibilities. Further, it will ensure that corporations are continually blamed for all societal problems, as The New Yorker cartoon jokingly does.

In reality it is the government's responsibility to address these societal problems and needs through regulation using areas other than corporate law. Corporations already help by creating jobs, stimulating business for suppliers and others they trade with, bringing products to consumers and offering returns to those who invested capital. Corporations should not be required to save the world in any other ways. Any such requirements, in addition to taking away from the company's actual business, will chill innovative programs that companies might otherwise have voluntarily initiated in favour of stakeholders because such actions would no longer distinguish them from other corporations.

6. Future-proofing board decisions

The argument thus far in this article is that State interference through a vaguely defined corporate purpose is not efficient and should be avoided. However, this is not to say that corporations should be discouraged from incorporating ethical and social considerations within their decision-making. As discussed above, our current conception of the corporate purpose is wide enough for corporations to legitimately pursue the interests of other stakeholders. Business executives today are not only attuned to societal problems but also to stakeholder expectations that they should pay attention to these problems and needs.[88] Amazon pledged, on

[88] In the context of environmental law, Gunningham et.al. find that corporations going beyond compliance with the law can be explained by the interplay between social pressures and economic constraints. See generally Neil Gunningham and Robert A Kagan and Dorothy Thornton, 'Social License and Environmental Protection: Why Businesses Go beyond Compliance' (2004) 29 Law & Soc Inquiry 307 – 341.

the day of global protests demanding action on climate change, to become carbon neutral by 2040.[89] According to Amazon's CEO, Jeff Bezos, other business leaders may join him in taking the pledge.[90] Further, a consideration of stakeholder interests ensures that the corporation can avoid costly litigation or reputational damage[91] in future. For instance, had Uber had an effective way of dealing with sexual harassment claims internally, it could have avoided the public relations disaster that resulted from an employee's blog post about such issues.[92] This means that even where there is a gap in State regulation, prudent directors would consider both investor expectations[93] and societal expectations while assessing reputational risks associated with a particular decision.

Armour has used the term 'forward compliance' in the context of regulatory lag for data driven technologies.[94] He argues that it is desirable for firms to have internal policies and risk assessment guidelines that are more demanding than the current state of regulation because the fact that there is a gap in regulation will not save the firm's reputation when its actions cause harm to some section of society.[95] Similarly, Gadinis and Miazad, based on their study propose that companies see ESG[96] (environment, sustainability and governance issues) as a risk-mitigation process.[97] In the process of addressing ESG issues, companies consult with various stakeholders through which the company gains insights and perspectives it would not otherwise

[89] 'Amazon pledges to be carbon neutral by 2040' *The Business Times* (20 September 2019) < https://www.businesstimes.com.sg/technology/amazon-pledges-to-be-carbon-neutral-by-2040>.
[90] Ibid.
[91] In a recent Australian case, it was suggested that reputational damage might constitute harm to a company's interests. See ASIC v Cassimatis (No 8) [2016] FCA 1023 at [481]-[483].
[92] See Akshaya Kamalnath, 'Corporate Diversity 2.0: Lessons from Silicon Valley's Missteps' (2018) 20 Or Rev Int'l L 113.
[93] Ann Lipton notes that many investors may care about things other than financial returns. However, she points out that in case of false corporate disclosures, investors may only seek damages to the extent that they can prove they experienced monetary losses as a result of such false disclosures. See Ann Lipton, "Mixed company – The Audience for Sustainability Disclosures" forthcoming in The Georgetown Law Journal Online (2019) available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3402392> 84.
[94] John Armour, 'The case for 'forward compliance'' (2018) British Academy Review 19 available at <https://www.thebritishacademy.ac.uk/sites/default/files/BAR34-07-Armour.pdf>
[95] Ibid.
[96] The term ESG has come to replace CSR in many contexts.
[97] Stavros Gadinis and Amelia Miazad, 'Sustainability in Corporate Law' (2019) available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3441375>. On similar lines, Georgina Tsagas has proposed that the UK Corporate Governance Code should stipulate that board should initiate a dialogue with various stakeholders so as to give effect to the factors mentioned in section 172 of the Companies Act (UK). See Tsagas, G, 2017, 'Section 172 of the Companies Act 2006: Desperate Times Call for Soft Law Measures' in Nina Boerger and Charlotte Villiers (eds.) Shaping the Corporate Landscape Hart Publications, Forthcoming.

have.[98] These insights would help companies predict negative consequences of their operations or detect underlying problems that might have resulted in a future crisis.[99] Ultimately, protecting against problems that could arise in the future i.e. future proofing is what the long term shareholder value model calls for. At the same time, such future proofing would also be in line with the CSR model outlined by Sjåfjell and Sørensen where corporations internalise their business externalities. While this is not the main focus of this article, there may be ways to incentivise future-proofing by, for instance, requiring companies to disclose non-financial information to shareholders.[100] Although many jurisdictions already require such disclosures,[101] standard disclosure formats across jurisdictions would aid shareholder engagement.

Thus, corporations may become willing partners of the State in solving these problems either for ethical reasons or with a view to the future proofing of the corporation or simply for the enhancement of their reputation. While such willing collaborations or voluntary CSR (in terms of future proofing) or philanthropy is positive, what must be resisted at all costs is an upending of corporate law[102] as we know it because of State interference. The Indian experiment has shown that government might use CSR or a redefinition of the corporate purpose to require corporations to take on some of the government's own role. We would do well to take heed of the insights from India's CSR experience while assessing Senator Warren's proposal and other calls for widening of the 'corporate purpose'.

98 Gadinis and Miazad, Ibid.
99 Ibid.
[100] The author aims to explore incentives for future proofing in subsequent projects. Watch this space.
[101] For a discussion of non-financial disclosure obligations in the UK see Choudhury and Petrin (n. 31) 402 – 405. For a discussion of non-financial disclosure obligations in Australia see Jean du Plessis, 'Disclosure of non-financial information: A powerful corporate governance tool' (2016) 34 C&SLJ 69.
[102] According to William Bratton, "corporate law should facilitate corporate attempts to maximize productive output (and hence wealth) in a competitive economy, encouraging long-term investment at the lowest cost of capital, subject to exterior regulations that control externalities." See William W. Bratton, 'Framing a Purpose for Corporate Law', (2014) 39 J. Corp. L. 713.