Policy Design and Practice

ISSN: (Print) 2574-1292 (Online) Journal homepage: https://www.tandfonline.com/loi/rpdp20

Why comply with an unforced policy? The case of mandated corporate social responsibility in India

Panchali Guha

To cite this article: Panchali Guha (2020) Why comply with an unenforced policy? The case of mandated corporate social responsibility in India, Policy Design and Practice, 3:1, 58-72, DOI: 10.1080/25741292.2020.1726592

To link to this article: https://doi.org/10.1080/25741292.2020.1726592

Published online: 16 Feb 2020.

POLICY DESIGN AND PRACTICE
2020, VOL. 3, NO. 1, 58–72
https://doi.org/10.1080/25741292.2020.1726592

Why comply with an unenforced policy? The case of mandated corporate social responsibility in India

Panchali Guha

Lee Kuan Yew School of Public Policy, National University of Singapore (NUS), Singapore, Singapore

ABSTRACT

Can public policies achieve high compliance without resorting to high enforcement? The case of India's mandated corporate social responsibility law shows that they may be able to do so by leveraging the underlying motivations of policy targets. The law, introduced in 2013, requires large companies to spend at least 2% of their net profits on CSR. Despite no monitoring, enforcement, or penalties for noncompliance, it has resulted in significant increases in CSR spending by creating a social norm around the 2% target, and relying on social pressure and reputational effects, rather than government enforcement, for compliance. However, the case also shows that such an approach has attendant risks: relying on the social motivation of policy targets may alienate those with normative motivations, and weaknesses in the surrounding legal and institutional environment may enable some firms to disguise their noncompliance.

ARTICLE HISTORY
Received 9 November 2019
Accepted 31 January 2020

KEYWORDS
Policy compliance; policy target; motivation; social norm; corporate social responsibility; CSR; India

1. Introduction

When do policy targets willingly comply with a policy? This is clearly a question of great relevance to policy design, the cost-effectiveness of policy implementation, and eventual policy success or failure. It is therefore useful to understand the underlying attitudes and motivations for compliance among policy targets, and draw lessons from cases in which a public policy is able to leverage these underlying motivations to achieve a high rate of compliance with little or no enforcement.

One such case is that of the mandated corporate social responsibility (CSR) policy in India. India made it mandatory in 2013 for all companies above a certain size to spend at least 2% of their annual net profits on CSR. Despite zero monitoring, enforcement, or penalties for noncompliance, the policy has resulted in high (although by no means universal) CSR spending. The objective of this article is to examine the performance of the Indian mandated CSR policy in order to understand how it has achieved this remarkable result, and whether the observed increases in CSR expenditure have

CONTACT Panchali Guha panchali.guha@u.nus.edu Lee Kuan Yew School of Public Policy, National University of Singapore (NUS), Oei Tiong Ham Building, 469C Bukit Timah Road, Singapore 259772, Singapore

been accompanied by any undesirable or unanticipated consequences. Governments in both developed and developing countries have taken an increasing interest in recent years in using public policy to encourage CSR efforts by corporations (although few have gone as far as making CSR mandatory). In this context, the Indian case offers useful lessons on taking a regulatory approach to designing CSR policy.

The article is organized as follows. Section 2 introduces India's mandated CSR policy. Section 3 discusses the underlying motivations of policy targets and their relationship to policy compliance, and whether public policy can leverage underlying motivations to induce compliance. Section 4 summarizes the empirical evidence on the effects of the policy, while section 5 discusses the key implications of the evidence. Finally, section 6 concludes.

2. India's mandated CSR law

When the Indian government set about overhauling the Companies Act of 1956 after more than 50 years, one new provision created consternation in the corporate sector. This was the provision on mandated or compulsory CSR. Section 135 of the 2013 Companies Act (MCA 2013) mandates that every company with a net worth of Rs 500 crore[1] or more, or turnover of Rs 1000 crore or more, or a net profit of Rs 5 crore or more, should spend at least 2% of its average net profit (before tax) in the three preceding financial years on CSR annually.

In addition, the Act also stipulates the governance arrangements that companies are required to implement for their CSR activity. This includes the formation of a CSR committee, the role of which is to formulate and recommend a CSR policy to the company board. The company board is required to approve the CSR policy, ensure implementation of the CSR activities, and ensure compliance with the 2% target. It is also required to disclose the company's CSR policy in the annual report and on the official company website. If the company fails to comply with the 2% target, it is required to provide an explanation in its annual report.

The Act recommends areas of social and environmental development in which to deploy CSR funds. These include eradicating extreme hunger and poverty, reducing child mortality and improving maternal health, promoting education, promoting gender equality and women's empowerment, combating HIV, AIDS, malaria and other diseases, promoting environmental sustainability, contributing to the Prime Minister's National Relief Fund, etc. It also directs companies to give preference to the local area around their area of operation when disbursing funds.

Finally, the Act grants companies the option to implement CSR activities directly on their own, through their own nonprofit foundations, or through independently registered nonprofit organizations, provided these organizations have a track record of at least 3 years in similar activities.

What made the CSR law especially controversial, and its potential effects particularly uncertain, was that it was virtually unprecedented. India was only the third country in the world, after Indonesia and Mauritius, to mandate CSR; most CSR policies adopted elsewhere have taken the form of 'soft' interventions such as the introduction of voluntary CSR guidelines rather than 'hard' interventions such as mandatory targets

(Albareda et al. 2008). Indonesia was the first to adopt a mandatory approach, passing a law in 2007 that made it compulsory for companies operating in the field of natural resources to engage in, and report on, CSR activity. Unlike the Indian law, however, it did not specify a target level of CSR spending. It was also not accompanied by implementing regulations, making it "more inspirational in character than … any kind of operational regulation" (Waagstein 2011). Perhaps inevitably, the law has failed to result in CSR spending increases over previous voluntary levels (Chang 2018). On the other hand, the Mauritian law, introduced in 2009, was similar to India's as it also introduced a requirement for companies to spend 2% of their profits on CSR (although, unlike the Indian law, this requirement extended to all profitable companies regardless of their size). Lamentably, the lack of high-quality empirical evidence makes it difficult to compare its effects with those of the Indian law.

By directing companies to either comply with the 2% CSR spending requirement, or provide an explanation if they fail to do so, the Indian mandated CSR law favored a 'comply or explain' model of enforcement. Essentially, what this meant was that a firm's failure to comply with the 2% spending requirement did not automatically place it in violation of the law, as long as it was able to provide a 'reasonable' explanation (although what constituted a 'reasonable' explanation was not specified). It would, however, be in contravention of the law if it failed to provide an explanation. This put the mandated CSR law in the interesting position of being a compulsory regulation with zero enforcement (and consequently zero sanctions).

It is interesting to speculate briefly on why the Indian government took the unusual steps of (a) making CSR mandatory, and (b) implementing it with zero enforcement and sanctions. Let us first consider the question of why it was made mandatory. Despite being the world's fastest growing economy until recently, India continues to perform poorly on a wide range of social development metrics (Dreze and Sen 2013), with a rank of 129 out of 189 countries in the UN human development index rankings. 27.5% of its population still lives in multidimensional poverty, suffering deficits in basic living standards such as availability of safe drinking water, sanitation, nutrition, housing and education (Alkire et al. 2018). Meanwhile, income inequality has risen sharply in the last few decades, with the top 1% of the population currently capturing 22% of the nation's income (Chancel and Piketty 2019). The government may therefore have wanted to use the CSR law to rebalance the economy and increase the resources available for social development projects. The minister of corporate affairs noted at the time that full compliance with the law would generate an additional Rs 15,000–20,000 crore for development projects (*Business Today* 2013), while policy-makers referred to the law as a "historical opportunity" and a potential "game changer" for Indian development (Sarkar and Sarkar 2015).

The government may also have seen mandatory CSR as a way of getting firms to account for negative social and environmental externalities they create. It may also have wanted to avoid doing so via a tax, as corporate tax rates are already quite high in India (Jahnsen and Pomerleau 2017). Besides, public sector waste and inefficiency (Rayp and Van De Sijpe 2007), corruption (Desai 2018), disincentivised public officials (Afridi 2017), and lack of state capacity (Vaishnav et al. 2017) may have created a view within some sections of government that the private sector could do a more effective job of public good provision than the state.

The insertion of the mandated CSR clause may also have been a calculated attempt to avert a popular backlash, given that the rest of the 2013 Companies Act was extremely pro-business (Van Zile 2011). What is certainly evident is that there was a great deal of vacillation around it. After flirtations – with little or no effect – with voluntary CSR guidelines in 2009 and 2011 (Gatti et al. 2018), Manchiraju and Rajgopal (2017) report that the CSR clause was first inserted, along with a self-reporting requirement, into the draft Company's Bill in August 2010. When industry protested vociferously, the Ministry of Corporate Affairs announced in February 2011 that it was considering making CSR voluntary instead of compulsory. However, the government changed tack again in December 2011, and introduced the draft bill into the lower house of Parliament with the mandatory CSR clause re-inserted. This was the version of the bill that was subsequently approved by both houses of Parliament and became law in August 2013.

Let us now consider the second question: given that the government wanted to institute mandatory CSR, why did it decide to implement the policy with zero enforcement and sanctions? Again, there is no official explanation for this, but it may have been a compromise as a consequence of pushback from the corporate sector, which protested vehemently that such a move would impose an additional burden on businesses and remove the discretionary element of CSR. Critics objected that "A mandatory expenditure is a tax … This is a back-door way to increase corporate taxes without a transparent political debate" (Karnani 2013). Even philanthropists had their reservations: Azim Premji, the chairman of Wipro Limited who has donated more than half his personal wealth to charity, noted that "spending two per cent on CSR is a lot, especially for companies that are trying to scale up in these difficult times. It must not be imposed" (Pande 2013).

The government may also have realized that, given the social desirability and reputational aspects of the policy, hard enforcement was not required, and merely mandating the quantity of CSR would be sufficient to create incentives for compliance. If so, this view has a certain credence, as we will see below.

3. Target motivation, policy compliance, and the role of public policy

The literature on the underlying motivations of policy targets usually distinguishes between three types of motivations: economic, social and normative (Nielsen and Parker 2012; Winter and May 2001). The economic motivation has tended to be the de facto assumption about how policy targets determine their level of policy compliance (Howlett 2018); it assumes that policy targets select their preferred compliance level based on a rational optimization calculation of some objective function, subject to the perceived probability of detection and size of penalty if caught not complying. The social motivation relates to the need to earn the approval and respect of others. Although compliance in this scenario can also be broadly interpreted as stemming from some kind of cost-benefit calculation, the relevant costs and benefits here are social rather than financial, relating to the social advantages and disadvantages that the policy target perceives will follow from complying with or violating social norms. The normative motivation stems either from intrinsic moral agreement with the policy, or an intrinsic sense of duty to comply with government laws regardless of moral agreement.

Public policy can potentially be used to leverage the underlying motivations of policy targets. If the primary motivation is economic, policies that use positive and/or negative incentives, increase monitoring, and tighten enforcement are likely to be effective (Weaver 2014, 2015). If the primary motivation is social, policies that create, utilize or reinforce a social norm or expectation are likely to be useful. For instance, descriptive social norms – providing people with information about how others typically act in similar situations – have been found to be powerful ways to influence behavior (e.g. Gerber and Rogers 2009). Finally, if the primary motivation is normative, moral or normative injunctions can be used to induce compliance. Improving the quality of governance also helps to increase compliance by improving the perceived legitimacy of government (Levi and Sacks 2009).

Are there any potential risks associated with using public policies to increase policy compliance by leveraging underlying target motivations? First, the design of such policies is probably not straightforward. The target population is likely to have heterogenous motivations, and hence a mix of policy tools with different characteristics may be required to induce policy compliance (Weaver 2014; Howlett 2018).

Second, it is important to recognize the potential for unintended consequences, particularly when public policies wade into the business of trying to influence social norms. One of the more puzzling questions about social norms centers around why they emerge. One answer to this question comes from the signaling model of social norms, which theorizes that, in the longer run, social norms are costly signals that we use to identify ourselves as 'good' (socially responsible) rather than 'bad' (socially irresponsible) types, in order to induce other 'good' types to cooperate with us (Posner 2000). This raises the possibility that government intervention to create or strengthen a social norm may actually undermine the social motivation of some policy targets, who are now no longer able to signal their 'socially responsible' type as effectively as before due to the ubiquity of the signal.

Another kind of unintended consequence emerges if policies intended to achieve compliance via one kind of motivation have the effect of crowding out other kinds of motivations. The proposition that economic incentives or disincentives sometimes crowd out intrinsic motivation (Frey and Jegen 2001) has found empirical support in a wide range of contexts. For instance, a study conducted in Israeli day care centers found that the introduction of a fine on late pickups reduced parents' intrinsic motivation to arrive on time (Gneezy and Rustichini 2000), and an experiment which randomly offered monetary compensation to potential blood donors found that the supply of blood donation reduced sharply as a result (Mellström and Johannesson 2008).

Finally, it is problematic if features of the surrounding legal and institutional context create the space for certain types of noncompliance to emerge. Despite limited theoretical conceptualization of noncompliance in the public policy literature (Gofen 2015), it should be fairly obvious that different forms of noncompliance exist in the real world, including (but not limited to) simple refusal to comply, symbolic forms of compliance, and disguising noncompliance to look like compliance via some form of corruption or fraud. Conditional on underlying target motivation, formal and informal institutions may play an important role in fostering certain forms of noncompliance over others. The existence of loopholes in tax laws, for instance, can enable what McBarnet (2003) terms "creative compliance" to emerge, whereby individuals engage in tax avoidance that obeys the letter but evades the spirit of tax laws.

4. Empirical evidence on policy compliance with mandated CSR

The mandated CSR law came into effect on April 1, 2014. In the first year of implementation, 16,548 companies were subject to the mandate and spent a total of Rs 10,066 crore on CSR. By 2017–18, these numbers had increased to 21,397 companies and Rs 13,624 crores, respectively (National CSR portal n.d.). Not all of this expenditure may have represented new spending created by the law. Corporate giving has a long tradition in India: some of the older business houses such as the Tata, Birla, Bajaj and Godrej conglomerates have long been associated with philanthropy, as have more recent entities such as Infosys and Wipro. Compliance is unlikely to have posed challenges for such firms. In many other cases, however, commitments to social and environmental causes were opaque. In a 2007–2008 survey of the 500 largest Indian companies, only 49% were found to report on CSR, and the majority of these did not state their actual CSR expenditure in their balance sheets or annual reports (Gautam and Singh 2010). Where donations were made, they were sometimes very small in relation to firm size (Bansal and Rai 2014). Manchiraju and Rajgopal (2017) found that the passage of the law caused a 4.1% reduction in the stock prices of affected firms, suggesting that the law imposed significant new costs on most of them.

Based on sources detailed below, an examination of the empirical evidence on policy compliance with the law so far yields the following broad conclusions:

1. Overall, the law has resulted in sharp increases in CSR expenditures by policy targets. CSR expenditures have also been increasing over time.
2. However, smaller firms exhibit lower compliance than larger firms.
3. On average, firms that spent less than 2% on CSR before the law increased their spending after the law. On the other hand, firms that spent more than 2% on CSR before the law reduced their spending after the law.
4. Some firms over-comply by spending more than 2% on CSR.

These conclusions are elaborated below.

Overall, the law has resulted in sharp increases in CSR expenditures by policy targets. CSR expenditures have also been increasing over time. Data from the National CSR portal (n.d) show that the percentage of firms with positive CSR spending increased from 36% in 2014–2015 to over 50% in the next 2 years. While 17% of firms spent 2% or more of their profits on CSR in 2014–2015, 26% did so in 2017–2018. Among firms listed on the National Stock Exchange, average CSR expenditure as a percentage of net profits increased from 1.58% in 2014–2015 to 1.87% in 2017–2018 (PRIME Database, n.d.).

In its analysis of CSR by the top 100 listed companies, KPMG (2018) shows evidence of a strong rising trend in CSR spends over time, starting from 2014–15. Actual CSR expenditure by these companies as a proportion of prescribed expenditure increased from 79% in 2014–2015 to 90% in 2015–2016, 97% in 2016–2017, and over 100% in 2017–2018. The proportion of companies that spent less than the prescribed 2% of profits on CSR fell from 62% in 2014–2015 to 33% in 2017–2018, while the proportion of companies that exactly matched the 2% target increased from 5% in 2014–2015 to 20% in 2017–2018.

CII (2017, 2018) shows similar trends for companies listed on the Bombay Stock Exchange that fell within the ambit of the law. These companies collectively spent 80% of the prescribed expenditure in 2015–2016, increasing to 92% in 2016–2017 and 2017–2018. The percentage of companies that spent at least 2% on CSR increased from 52% in 2016–2017 to 58% in 2017–2018.

While the above sources only illustrate CSR trends in the years after the law was introduced, Dharmapala and Khanna (2018) compared the CSR spending of nearly 4000 firms before and after the law. They found that, while very few firms in their sample engaged in any CSR spending before the law, many started to spend on CSR after it: the probability of engaging in CSR increased by about 0.34 in the very first year of implementation. The law also had an effect on firms that already engaged in CSR prior to the law, as their spending levels increased by about Rs 6 million on average.

Bansal et al. (2019) investigated the effect of the law on the CSR activity of almost 40,000 firms in 2015 and 2016. They found that the law resulted in a statistically significant increase in the probability of CSR reporting: the probability that a firm would report its CSR spending increased by 0.15 in 2015 and 0.22 in 2016. It also had a positive and statistically significant effect on CSR spending, with the 2016 effect being larger than the 2015 effect. Consequently, CSR spending increased by Rs 72 billion and Rs 93 billion in 2015 and 2016 respectively, although there were still significant levels of under-compliance. On average, eligible firms spent about 1% of net profits on CSR.

However, smaller firms exhibit lower compliance than larger firms. When Dharmapala and Khanna (2018) restricted their analysis to smaller target firms (defined as firms with net profit of Rs 0–100 million) only, they found that the increase in the probability of engaging in CSR was much smaller at 0.05, although still statistically significant. This meant that, although the law made CSR spending more probable for both larger and smaller firms, the effect was more muted for smaller firms. Bansal et al.'s (2019) analysis also indicated that smaller firms spent a smaller proportion of their profits on CSR.

On average, firms that spent less than 2% on CSR before the law increased their spending after the law. On the other hand, firms that spent more than 2% on CSR before the law reduced their spending after the law. Analyzing changes in the CSR spending of a sample of firms listed on the Bombay Stock Exchange between 2008 and 2015, Mukherjee et al. (2018) found that most firms that did not spend anything on CSR before the law initiated CSR spending in 2014–2015, whether they were within the ambit of the law or not (although those that were spent more than those that were not).

In addition to their analysis on a large sample of almost 4000 firms, Dharmapala and Khanna (2018) also examined changes in CSR spending for a sub-sample consisting of 55 of the 100 largest firms in the country. Although the sample size is small, the results from this analysis are very intriguing. Of the 55 firms, 45 firms spent less than 2% of their net profit on CSR in fiscal year 2013–2014 (i.e. before the mandated CSR law came into effect). Once the law came into effect in 2014, these firms significantly increased their CSR spending in order to comply with the law. On the other hand, the remaining 10 firms spent more than 2% of their net profit on CSR in 2013–2014, prior to the imposition of the law. When the law made the 2% target mandatory in 2014, these firms actually responded by reducing their CSR expenditure.

This was also true of firms outside the CSR mandate. Mukherjee et al.'s (2018) analysis showed that firms that voluntarily spent on CSR before the law, but were not mandated to do so by the law, responded by reducing CSR spending. While these firms spent about 3.87% of profits on average on CSR before the passage of the law, they spent 3.53% of profits on it in 2014–2015.

Some firms over-comply by spending more than 2% on CSR. Analysis of CSR spending by the top 100 listed companies showed that, while 33% of them spent more than 2% of profits on CSR in the first year of implementation of the law in 2014–2015, this proportion increased to 47% by 2017–2018 (KPMG 2018). Bhattacharyya and Rahman (2019) found that, overall, 25% of their sample of 1,516 firms over-complied with the law. Government data (MCA n.d.) indicates that the actual CSR expenditure of some companies considerably exceeds prescribed amounts. For instance, by 31st January 2016, Reliance Industries had already spent Rs 228 crore over and above its mandated expenditure for 2015–2016. Oil India and Tata Steel similarly exceeded prescribed levels by Rs 35 crores and Rs 3 crores, respectively.

5. Discussion

Are the observed empirical facts consistent with heterogenous target motivations? As a starting point, assume that policy targets are motivated by a mix of economic, social and normative considerations. Let us first consider the group of firms that are primarily motivated by rational or economic considerations. What would we expect to observe regarding their compliance with the mandated CSR law? Economic theory predicts that a rational, profit-maximizing firm will comply up to the point at which it receives a marginal benefit of one rupee from spending an additional rupee on CSR. If it receives a higher marginal benefit, it is in the firm's interest to increase its CSR spending and obtain a positive net benefit. On the other hand, if it receives a lower marginal benefit, it is in its interest to cut back on its CSR spending in order to avoid a net loss.

In general, the marginal benefit of compliance can be expected to consist of the private benefit from compliance as well as the expected avoided cost of noncompliance. In most regulatory contexts, the expected avoided cost of noncompliance would be calculated as the cost of penalties for noncompliance, multiplied by the probability of detection. However, as already noted, in the case of the Indian mandated CSR policy, there was zero monitoring of whether firms actually complied with the 2% requirement, and hence zero penalties if they did not. Therefore, the expected avoided cost of noncompliance was zero.

What about the private benefit from compliance? Firms engaged in CSR may enjoy a positive reputational effect, inspiring more favorable evaluations of the firm and its products, greater goodwill and loyalty, and eventually higher profitability (Aguinis and Glavas 2012; Orlitzky et al. 2003). In the Indian context, however, given that CSR levels before the law were low and most target firms saw the law as an imposition and a burden, it seems reasonable to infer that many firms would not perceive the reputational benefits as being high enough to justify spending 2% of their net profits on CSR, in the absence of policy enforcement. This explains why full compliance with the policy is far from universal.

The real puzzle here, however, is not why some companies refused to comply fully, but why the rest did. It is likely that, by setting the 2% target, the government created a powerful new social norm or expectation, which firms were hesitant to violate.[2] This is certainly consistent with the empirical evidence on the sharp rise in CSR spending after the law.

A logical proposition that follows from this is that the social cost of noncompliance with the norm is not likely to be the same for all types of firms. The larger and more visible the firm, the more salient reputation and visibility is likely to be, and hence the higher the sensitivity to the social cost of violating the social norm. This is borne out by the empirical evidence. As noted in section 4, smaller firms have tended to be less compliant than larger ones.

Next, let us consider the implications of potential crowding-out in this context. It is possible that making CSR a mandatory activity may crowd out the intrinsic motivation to engage in it. Empirical evidence that would be consistent with this hypothesis would be to observe firms that spent more than 2% of their net profits on CSR before the law actually reduce their CSR spending after the law, as a form of protest.

As stated in section 4, there is some empirical evidence in favor of this, as some firms that spent more than 2% before the law did reduce their spending after the law. However, it is difficult to ascertain solely from the data whether this represents a crowding-out of intrinsic motivation, as it is also consistent with a 'weak' social motivation under the signaling model of social norms. Before the passage of the law, a firm that wanted to signal its 'socially responsible' type could do so by voluntarily engaging in CSR. It is plausible to speculate that what such firms do after the law depends on the intensity with which they want to signal their 'socially responsible' type. A firm that is content with a weak signal would, if its initial CSR spend was less than 2%, raise CSR spending to the target level, and then stop. On the other hand, if its initial CSR spend was more than 2% to begin with, it might choose to respond by reducing it down to the target level of 2%. On the other hand, a firm that wants to send a strong signal of type and to distinguish itself from other 'socially responsible' types may choose to do so by over-complying, i.e. spending more than the required 2% on CSR. Both patterns of behavior have been observed in the data.

Finally, we must consider the possibility of corruption or fraud as a behavioral response on the part of firms that do not have an intrinsic motivation to comply with the policy, but feel compelled to avoid the social costs associated with open noncompliance. Within the context of voluntary CSR, firms have been known to cheat, or engage in CSR activities that are more window dressing than substantive social contributions

(Andrews 2016; Frynas 2005). In the Indian case, there are disturbing indications that the unfortunate combination of the mandatory CSR spending requirement, the lack of monitoring mechanisms within the law, and lack of overarching regulation in the non-profit sector may be leading to similar problems.

The non-governmental sector in India is very large: estimates of the total number of NGOs in the country range from two million (Bornstein and Sharma 2016) to over three million (Srinath 2018). The sector is also poorly regulated. Srinath (2018) states that "civil society in India is still governed by a hodgepodge of laws, many dating back to colonial times", and Sundar (2017) highlights the urgent need for comprehensive legal reform of the nonprofit sector.

The risk of fraud inherent in the CSR regulations was flagged early by prominent industrialist and philanthropist Ratan Tata, who warned that "You'll see an enormous growth in NGOs, everybody tripping over themselves in order to register to attract some of this money … You will have a registered NGO, you will have the money, the money goes to the NGO and it may be 3 or 4 years before the whole thing explodes in a series of fraudulent operations, money being given to people that don't exist, or causes that are subterfuge for something else" (White 2014).

Recent media reports suggest that this is coming to pass, with the CSR law enabling fraud, money laundering and other unethical practices. One news article explained a typical route for fabricating CSR spending: "If a company is obligated to spend, say, Rs 10 crore on CSR, it writes out a cheque in favor of a trust that works in education, healthcare, environment protection or any of the activities specified by the government. The trust, after deducting its commission, discreetly returns the money in cash to the officials or promoters… " (Narayanan 2015). In other instances, those responsible for handling CSR allocations within companies direct funds to NGOs or trusts run by relatives or friends, inflate CSR expenditures, or are defrauded by implementation partners (Singh 2019; Ahuja 2017; Yathiraju 2018). Yet other reports indicate that firms may be using CSR expenditures to gain favor with the government by investing in its pet projects – such as monumental statues and cow shelters – rather than on projects that are truly socially beneficial (Sundar 2018).[3] Krichewsky (2017) explains how such CSR benefits both the involved firm and its political patron: "Companies secure the support of elected representatives by letting them influence the allocation of CSR resources in their constituency, while elected representatives improve their popularity by displaying their influence in public, for instance during speeches in inauguration ceremonies of CSR-funded projects".

6. Conclusion

The aim of this article was to examine the performance of India's mandated CSR policy in order to draw out useful policy lessons on (a) how it has resulted in high levels of policy compliance despite zero monitoring, enforcement, or penalties for noncompliance, and (b) whether these gains have come at the expense of any undesirable or unanticipated consequences. The case illustrates that it is possible for a policy to achieve a high rate of compliance without resorting to vigorous monitoring and enforcement, creating a social norm. Despite relying simply on a "comply or explain" approach to enforcement, the policy has resulted in a sharp increase in CSR spending by target firms. Compliance has also increased over time, illustrating the self-reinforcing nature of social norms (Nyborg et al. 2016).

On the other hand, there are indications that these gains have come at a cost. First, some firms that spent more than 2% before the law responded by spending less than 2% after it, which is clearly not the desired behavioral response from society's perspective. Second, media reports suggest that some unscrupulous firms may be colluding with NGOs to create fraudulent CSR projects.

From a theoretical perspective, the case is interesting because it illustrates that policy designs that match policy tools to the underlying motivations of policy targets can generate compliance even in the absence of enforcement. Hence, it explores the relationship between target motivation and policy compliance, which has been highlighted as a key research gap in the public policy literature (Howlett 2018; Capano and Howlett 2019).

It is also interesting as it offers potential – although not conclusive – support for the crowding-out hypothesis in target motivation. One possible explanation for why firms that spent more than 2% before the law reduced spending after it is that making CSR mandatory introduced a legal and social motivation to comply that crowded out their intrinsic motivation for compliance (an alternative explanation, which cannot currently be ruled out, is that such firms decided to jettison CSR as an effective mechanism for demonstrating their quality once it became ubiquitous). It also illustrates the importance of the surrounding legal and institutional context in enabling certain forms of noncompliance to emerge. In the Indian case, the most important contextual factor is likely to have been the weak regulation of the nonprofit sector, which enabled disguised noncompliance to emerge.

The case has useful implications for other jurisdictions that may want to adopt a regulatory approach to CSR in future. It illustrates that a policy does not always have to rely on intensive monitoring and enforcement to achieve compliance; if it is successful at instituting a social norm, it can rely on peer pressure and reputational effects to do the heavy lifting instead. While government efforts to institute social norms are not likely to be uniformly successful, factors that are likely to work in the government's favor in the case of CSR include the co-creation of private benefits to firms from CSR efforts, and a general shift in societal attitudes that places greater emphasis on the social responsibilities of firms.

On the other hand, the case also highlights the need to take account of heterogenous target motivations when designing CSR policy, as it shows that a policy that induces the desired behavioral response in one target group may well create undesirable behavioral responses in another. Finally, it illustrates the dangers of ignoring weaknesses in the surrounding legal and institutional context when designing policy. Certainly in the Indian context, the inconsistent regulation of the nonprofit sector is an issue that requires attention, not only from the CSR perspective, but also because of the reputational risk to the entire sector from the fraudulent activities of a few.

As a postscript, note that, despite the considerable increases observed in CSR spending after the introduction of the law, the Indian government has recently taken steps to reinforce its mandatory nature in order to further increase compliance. An amendment to the Companies Act introduced on July 31, 2019 requires firms to transfer any unspent CSR funds to a special CSR account and to spend the funds within the next 3 years, failing which the funds must be transferred to one of the funds specified in the Act. The amendment also introduced penal provisions for noncompliance, although the government then backpedaled in the face of industry alarm, and has currently opted to treat noncompliance as a civil liability rather than a criminal offense (PTI 2019).

Notes

1. A crore is a commonly used monetary unit in India which is equivalent to ten million. Based on the exchange rate in January 2020, Rs 1 crore approximately equals US $0.14 million.
2. Bansal et al. (2019) also allude to the 2% target as a social norm. However, they argue that the desire to conform with the social norm is an extrinsic motivator that replaced firms' intrinsic motivation of keeping up with their peers. This argument ignores the importance of maintaining one's reputation among one's peers as an important factor driving the self-reinforcing nature of the social norm. Characterising the desire to imitate one's peers as intrinsic motivation is also not consistent with the way in which intrinsic motivation is usually conceptualised in the public policy literature.
3. Dharmapala and Khanna (2018) also allude to the possibility of corruption and fraud, but take the view that these are not likely to be widespread problems, on the basis that (a) firms can opt for non-compliance within the 'comply or explain' framework of the law, and (b) India's vibrant business press would catch instances of corruption or fraud. This article argues that open non-compliance is problematic for firms despite the 'comply or explain' model, due to the difficulties associated with openly violating a social norm. It also contends that lack of regulation of the non-profit sector makes it difficult to catch instances of corruption and fraud.

Acknowledgements

I am grateful to M Ramesh, two anonymous reviewers, and seminar participants at IPPN 2019 for their helpful feedback.

Disclosure statement

No potential conflict of interest was reported by the author(s).

ORCID

Panchali Guha http://orcid.org/0000-0001-8030-7798

References

Afridi, F. 2017. "Governance and Public Service Delivery in India." International Growth Centre, synthesis paper S-35407-INC-1. https://www.isid.ac.in/~fafridi/doc/igc_synthesis.pdf

Aguinis, H., and A. Glavas. 2012. "What We Know and Don't Know about Corporate Social Responsibility: A Review and Research Agenda." *Journal of Management* 38 (4): 932–968. doi:10.1177/0149206311436079.

Ahuja, R. 2017. "CBI Files FIR Against Corporate Lobbyist, NGO Over Misuse of CSR Funds." *Hindustan Times*. https://www.hindustantimes.com/india-news/cbi-files-fir-against-corporate-lobbyist-ngo-over-misuse-of-csr-funds/story-278i8W6UCK8l2hIdl8lr0M.html.

Albareda, L., J. M. Lozano, A. Tencati, A. Midttun, and F. Perrini. 2008. "The Changing Role of Governments in Corporate Social Responsibility: drivers and Responses." *Business Ethics: A European Review* 17 (4): 347–363. doi:10.1111/j.1467-8608.2008.00539.x.

Alkire, S., C. Oldiges, and U. Kanagaratnam. 2018. Multidimensional poverty reduction in India 2005/6–2015/16: Still a long way to go but the poorest are catching up. OPHI Research in Progress 54a, University of Oxford.

Andrews, N. 2016. "Challenges of Corporate Social Responsibility (CSR) in Domestic Settings: An Exploration of Mining Regulation Vis-à-Vis CSR in Ghana." *Resources Policy* 47: 9–17. doi:10.1016/j.resourpol.2015.11.001.

Bansal, S., M. Khanna, and J. Sydlowski. 2019. "Incentives for Corporate Social Responsibility in India: Mandate, Peer Pressure and Crowding-Out Effects." https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3370838.

Bansal, S., and S. Rai. 2014. "An Analysis of Corporate Social Responsibility Expenditure in India." *Economic and Political Weekly* 49 (50). https://www.epw.in/journal/2014/50/web-exclusives/analysis-corporate-socialresponsibility-expenditure-india.html

Bhattacharyya, A., and M. L. Rahman. 2019. "Mandatory CSR Expenditure and Firm Performance." *Journal of Contemporary Accounting & Economics* 15 (3): 100163. doi:10.1016/j.jcae.2019.100163.

Bornstein, E., and A. Sharma. 2016. "The Righteous and the Rightful: The Technomoral Politics of NGOs, Social Movements, and the State in India." *American Ethnologist* 43 (1): 76–90. doi:10.1111/amet.12264.

Business Today 2013. "Sachin Pilot Urges Companies to See CSR as Investment, Not Burden." https://www.businesstoday.in/current/corporate/sachin-pilot-on-corporate-social-responsibility-companies-act/story/198487.html

Capano, G., and M. Howlett. 2019. "The State of Policy Instrument Analysis: Knowns, Unknowns and the Current Research Agenda." https://www.ippapublicpolicy.org/file/paper/5cffe795eb233.pdf.

Chancel, L., and T. Piketty. 2019. "Indian Income Inequality, 1922–2015: From British Raj to Billionaire Raj?" *Review of Income and Wealth* 65 (S1): S33–S62. doi:10.1111/roiw.12439.

Chang, S. E. 2018. "Has Indonesia's Unique Progressivism in Mandating Corporate Social Responsibility Achieved Its Ends?" *Sriwijaya Law Review* 2 (2): 131–151. doi:10.28946/slrev.Vol2.Iss2.131.pp131-151.

Confederation of Indian Industry (CII) 2017. "Annual CSR Tracker 2016." www.cii.in.

Confederation of Indian Industry (CII) 2018. "Annual CSR Tracker 2017." www.cii.in.

Desai, R. D. 2018. "India continues to rank among most corrupt countries in the world". *Forbes*. https://www.forbes.com/sites/ronakdesai/2018/03/07/india-continues-to-be-one-of-the-most-corrupt-countries-in-the-world/#6160bb1179c6.

Dharmapala, D., and V. Khanna. 2018. "The Impact of Mandated Corporate Social Responsibility: Evidence from India's Companies Act of 2013." *International Review of Law and Economics* 56: 92–104. doi:10.1016/j.irle.2018.09.001.

Dreze, J., and A. Sen. 2013. *An Uncertain Glory: India and Its Contradictions*. Princeton, NJ: Princeton University Press.

Frey, B. S., and R. Jegen. 2001. "Motivation Crowding Theory." *Journal of Economic Surveys* 15 (5): 589–611. doi:10.1111/1467-6419.00150.

Frynas, J. G. 2005. "The False Developmental Promise of Corporate Social Responsibility: Evidence from Multinational Oil Companies." *International Affairs* 81 (3): 581–598. doi:10.1111/j.1468-2346.2005.00470.x.

Gatti, L., B. Vishwanath, P. Seele, and B. Cottier. 2018. "Are We Moving Beyond Voluntary CSR? Exploring Theoretical and Managerial Implications of Mandatory CSR Resulting from the New Indian Companies Act." *Journal of Business Ethics* 142: 1–2. doi:10.1007/s10551-018-3783-8.

Gautam, R., and A. Singh. 2010. "Corporate Social Responsibility Practices in India: A Study of Top 500 Companies." *Global Business and Management Research: An International Journal* 2 (1): 41–56.

Gerber, A. S., and T. Rogers. 2009. "Descriptive Social Norms and Motivation to Vote: everybody's Voting and So Should You." *The Journal of Politics* 71 (1): 178–191. doi:10.1017/S0022381608090117.

Gneezy, U., and A. Rustichini. 2000. "A Fine is a Price." *The Journal of Legal Studies* 29 (1): 1–17. doi:10.1086/468061.

Gofen, A. 2015. "Reconciling Policy Dissonance: Patterns of Governmental Response to Policy Non-Compliance." *Policy Sciences* 48 (1): 3–24. doi:10.1007/s11077-014-9202-9.

Howlett, M. 2018. "Matching Policy Tools and Their Targets: Beyond Nudges and Utility Maximisation in Policy Design." *Policy & Politics* 46 (1): 101–124.

Jahnsen, K., and K. Pomerleau. 2017. *Corporate Income Tax Rates Around the World, 2017, Tax Foundation Fiscal Fact No. 559*. Washington, DC: The Tax Foundation. https://files.taxfoundation.org/20170907092820/Tax-Foundation-FF559.pdf

Karnani, A. 2013. "Mandatory CSR in India: A Bad Proposal." Stanford Social Innovation Review. https://ssir.org/articles/entry/mandatory_csr_in_india_a_bad_proposal

KPMG 2018. "India's CSR Reporting Survey 2018." https://assets.kpmg/content/dam/kpmg/in/pdf/2019/01/India_CSR_Reporting_Survey_2018.pdf

Krichewsky, D. 2017. "CSR Public Policies in India's Democracy: Ambiguities in the Political Regulation of Corporate Conduct." *Business and Politics* 19 (3): 510–547. doi:10.1017/bap.2017.2.

Levi, M., and A. Sacks. 2009. "Legitimating Beliefs: sources and Indicators." *Regulation & Governance* 3 (4): 311–333. doi:10.1111/j.1748-5991.2009.01066.x.

Manchiraju, H., and S. Rajgopal. 2017. "Does Corporate Social Responsibility (CSR) Create Shareholder Value? Evidence from the Indian Companies Act 2013." *Journal of Accounting Research* 55 (5): 1257–1300. doi:10.1111/1475-679X.12174.

McBarnet, D. 2003. "When Compliance is Not the Solution but the Problem: From Changes in Law to Changes in Attitude." In *Taxing Democracy: Understanding Tax Avoidance and Evasion*, edited by V. Braithwaite. Aldershot, UK: Ashgate.

Mellström, C., and M. Johannesson. 2008. "Crowding out in Blood Donation: Was Titmuss Right?" *Journal of the European Economic Association* 6 (4): 845–863. doi:10.1162/JEEA.2008.6.4.845.

Ministry of Corporate Affairs (MCA) 2013. "The Companies Act, 2013". http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf

Ministry of Corporate Affairs (MCA). n.d. Accessed January 7 2020. http://www.mca.gov.in/MinistryV2/csrdatasummary.html

Mukherjee, A., R. Bird, and G. Duppati. 2018. "Mandatory Corporate Social Responsibility: The Indian Experience." *Journal of Contemporary Accounting & Economics* 14 (3): 254–265. doi:10.1016/j.jcae.2018.06.002.

Narayanan, D. 2015). "How Indian companies are misusing public trusts to launder their CSR spending." *The Economic Times,* October 21. https://economictimes.indiatimes.com/news/economy/finance/how-indian-companies-are-misusing-public-trusts-to-launder-their-csr-spending/articleshow/49474584.cms

National CSR Portal. n.d. Accessed January 7 2020. https://www.csr.gov.in/

Nielsen, V. L., and C. Parker. 2012. "Mixed Motives: Economic, Social, and Normative Motivations in Business Compliance." *Law & Policy* 34 (4): 428–462. doi:10.1111/j.1467-9930.2012.00369.x.

Nyborg, K., J. M. Anderies, A. Dannenberg, T. Lindahl, C. Schill, M. Schlüter, W. N. Adger, et al. 2016. "Social Norms as Solutions." *Science* 354 (6308): 42–43. doi:10.1126/science.aaf8317.

Orlitzky, M., F. L. Schmidt, and S. L. Rynes. 2003. "Corporate Social and Financial Performance: A Meta-Analysis." *Organization Studies* 24 (3): 403–441. doi:10.1177/0170840603024003910.

Pande, S. 2013. "Two per cent of profits on CSR activities is a lot, says Azim Premji." *Business Today*, September 26. https://www.businesstoday.in/current/corporate/azim-premji-aima-convention-corporate-social-responsibility/story/198960.html

Posner, E. A. 2000. "Law and Social Norms: The Case of Tax Compliance." *Virginia Law Review* 86 (8): 1781–1819. doi:10.2307/1073829.

Press Trust of India (c). 2019. "CSR violations not to be treated as criminal offence, says Nirmala Sitharaman." *India Today*, August 23. https://www.indiatoday.in/business/story/csr-violations-not-to-be-treated-as-criminal-offence-says-nirmala-sitharaman-1590896-2019-08-23

PRIME Database. n.d. "CSR spend by companies listed on NSE crosses INR 10,000 crore in 2017-18: nseinfobase.com." Accessed January 7 2020. https://www.primedatabase.com/DOC_EMAIL/CSR%20Report_nseinfobase.com_2017-18.pdf

Rayp, G., and N. Van De Sijpe. 2007. "Measuring and Explaining Government Efficiency in Developing Countries." *The Journal of Development Studies* 43 (2): 360–381. doi:10.1080/00220380601125230.

Sarkar, J., and S. Sarkar. 2015. "Corporate Social Responsibility in India—an Effort to Bridge the Welfare Gap." *Review of Market Integration* 7 (1): 1–36. doi:10.1177/0974929215593876.

Singh, A. 2019. "Unlocking value from CSR by mitigating fraud risks." *Hindustan Times*, September 15. https://www.hindustantimes.com/business-news/unlocking-value-from-csr-by-mitigating-fraud-risks/story-nn1cOJyBJqgRVTvYGBumeI.html

Srinath, I. 2018. "Citizen voices need to be heard in a democracy." *Hindustan Times*. https://www.hindustantimes.com/analysis/citizen-voices-need-to-be-heard-in-a-democracy/story-5tqZYe9sNnzrxvcadz14kL.html

Sundar, P. 2017. Why India's non-profit sector needs comprehensive legal reform. *The Wire*, May 10. https://thewire.in/politics/ngo-fcra-legal-reform

Sundar, P. 2018. Using CSR funds for political gain. *The Wire*, December 22. https://thewire.in/business/modi-government-csr-political-gain

Vaishnav, M., P. B. Mehta, and D. Kapur. 2017. *Weak Public Institutions behind India's Low State Capacity*. Washington, DC: Carnegie Endowment for International Peace. https://carnegieendowment.org/2017/05/15/weak-public-institutions-behind-india-s-low-state-capacity-pub-69971.

Van Zile, C. 2011. "India's Mandatory Corporate Social Responsibility Proposal: Creative Capitalism Meets Creative Regulation in the Global Market." *Asian-Pacific Law & Policy Journal* 13: 269.

Waagstein, P. R. 2011. "The Mandatory Corporate Social Responsibility in Indonesia: Problems and Implications." *Journal of Business Ethics* 98 (3): 455–466. doi:10.1007/s10551-010-0587-x.

Weaver, R. K. 2014. "Compliance Regimes and Barriers to Behavioral Change." *Governance* 27 (2): 243–265. doi:10.1111/gove.12032.

Weaver, R. K. 2015. "Getting People to Behave: Research Lessons for Policy Makers." *Public Administration Review* 75 (6): 806–816. doi:10.1111/puar.12412.

White, A. 2014. India CSR law could open door to fraud, says Ratan Tata. *Philanthropy Age*, February 2. Retrieved from http://www.philanthropyage.org/society/india-csr-law-could-open-door-fraud-says-ratan-tata

Winter, S. C., and P. J. May. 2001. "Motivation for Compliance with Environmental Regulations." *Journal of Policy Analysis and Management* 20 (4): 675–698. doi:10.1002/pam.1023.

Yathiraju 2018. 45 per cent of CSR funding paid to activist as 'consultation fee' to avail funds. *The New Indian Express*, July 15. Retrieved from http://www.newindianexpress.com/states/karnataka/2018/jul/15/45-per-cent-of-csr-funding-paid-to-activist-as-consultation-fee-to-avail-funds-1843525.html