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NSE-IGIDR International Conference on Corporate Governance

Edited Transcript
of

Keynote Speech and Panel Discussion

Mumbai
March 23, 2017

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Preface

While in maintaining and raising corporate governance standards, the onus lies with *all* the stakeholders, stock exchanges play a particularly key role, given their traditional mandate to monitor their listed companies' compliance with the listing and disclosure norms. In this respect, NSE has been no exception. Indeed, going beyond the regular channel of monitoring compliance with governance norms, NSE has taken initiatives to influence policy debates by involving regulators, practitioners and academics. NSE's collaboration with Indira Gandhi Institute of Development Research (IGIDR) for research on corporate governance is one such initiative, whose aim is to provide a platform for industry and academia to complement each other and to give research support for effective policy making. The third annual NSE-IGIDR conference on corporate governance held on March 23-24, 2017 in Mumbai was part of this initiative. The conference inter alia involved a keynote speech by Dr. Krishnamurthy Subramanian (Associate Professor of Finance at Indian School of Business), a presentation by Dr. Jayati Sarkar (Professor of Economics at IGIDR) and a panel discussion.

In his keynote speech, Professor Subramanian who was a member of the P.J. Nayak committee on governance of bank boards, focused on governance issues in the Indian banking sector. He stressed the point that the main factor that has ailed the public sector banks is their weak governance and highlighted two key ways in which public sector bank governance gets abused. One relates to the selection process of directors on the public sector bank boards; and the other to the micro-management of day-to-day operations of the public sector banks by bureaucrats. Dr. Subramanian explained that such intervention have led to asset growth without adequate prudence in lending, which in turn has resulted in a substantial increase in non-performing assets. In addition, public sector banks are systemically much riskier as compared to their private counterparts. The responsibility for correcting the situation lies primarily with the Government through radical reforms. However, the 'Indradhanush' set of reforms the government had announced in August 2016 has hardly been initiated.

As a prelude to the panel discussion on "Moving Ahead with Corporate Social Responsibility", Dr. Jayati Sarkar presented her research findings on evolution of CSR in India. An eminent set of panelists analyzed the mandatory CSR regime and compared it with the voluntary CSR regime. After becoming mandatory, CSR has become a topic of increasing interest among policymakers. How has CSR evolved over time in India, what has been the corporate experience after CSR has become mandatory and what are the implementation issues are some of the questions that were discussed.

I would like to thank all the panelists for their valuable contribution. I am also grateful to Professor Jayati Sarkar for her presentation and also for playing a wonderful role as the moderator in the panel discussion. The deliberations of the conference has been captured in this edited transcript and we believe that the transcript would be useful for industry participants, academics and policy makers.

Nirmal Mohanty
Chief Economist and Senior Vice President
National Stock Exchange of India Ltd.

Welcome Remarks

Mr. J. Ravichandran, MD and CEO in-charge, NSE

Somroop Mukherjee: Ladies and Gentlemen, Good Evening. I invite the MD and CEO in charge of NSE – Mr. J. Ravichandran to deliver the welcome address and start the conference.

Professor Krishnamurthy Subramanian – Indian School of Business, Professor Jayati Sarkar – IGIDR, Distinguished Panelists, Ladies and Gentlemen. I welcome you all to the third NSE-IGIDR International Conference on Corporate Governance. We have among us today many distinguished professionals, academics, senior officials from regulatory bodies besides NSE officials.

It is heartening to see so many of you finding time to come for this conference, some of you have come from outstation and some even abroad. We really appreciate this and hope that the conference will deliver value for your time and the efforts that we are going to spend here.

Many of you may already be aware about the background of this conference. A couple of years ago we entered into a research collaboration with Indira Gandhi Institute for Development Research in the area of corporate governance. Under this collaboration, we hold an annual conference and this annual conference is the third in this series.

Stock exchanges all over the world play a key role in maintaining and raising corporate governance standards of their listed companies. They do so by monitoring their listed company's compliance with the listing and disclosure requirements, part of which relate to governance norms. Now this is by way of regulatory mandate. We at NSE consider it prudent to go beyond these traditional channels by taking initiatives to influence policy debates in the country by involving regulators, practitioners and academics.

Towards this objective, our collaboration with IGIDR provides a platform for academics and practitioners complementing each other. Although it is a major initiative by NSE in the area of corporate governance, it is not the only one. NSE's interest in corporate governance comes from the fact that sound corporate governance in listed companies protects investor interest, bolsters their confidence in the market and NSE's commercial and regulatory objectives are better served when the integrity of the market improves.

Good corporate governance is key to the integrity of companies, financial institutions and markets, and even central to the health of any economy and its stability. Over the last one and a half decade, NSE has accorded increasing importance to raising corporate governance standards in the country and has taken several initiatives in promoting the same. The market has responded positively to these initiatives.

The impact of these initiatives has been encouraging. According to Ease of Doing Business report 2017, published by World Bank, in the index of Ease of Doing Business India's rank is 13^{th} in protecting minority investors, which is a component of the overall index and this is highly creditable. Over the last few years, India's ranking in this respect has remained consistently high. Needless to say that protecting minority investors is one of the key objectives of securities market regulations in India where concentrated ownership dominates the corporate landscape. In addition, the CG Watch 2016 published by CLSA and Asian Corporate Governance Association ranks India 7th among Asian countries in terms of overall CG score. This is no mean achievement. Of course, there is no room for complacency. A number of governance issues still remain and they manifest themselves periodically.

Coming back to the legal and regulatory initiatives, three prominent regulatory mandates in the recent past are noteworthy: To have at least one woman director on the board, spend on corporate social responsibility and board evaluation. NSE has supported these initiatives by way of conducting debates, undertaking advocacy and monitoring compliance. For example, in the last year's conference, we had a panel discussion on gender diversity on corporate boards. We also conducted a training program for women directors last year. Research has shown that higher gender diversity on boards improves corporate boards' effectiveness. Hopefully, governmental and SEBI initiatives and complimentary efforts by others, including us, will go a long way. Similarly, we had conferences on board evaluation where directors of several listed companies were invited. Historically, board evaluation in India, barring a few large companies, is not commonplace. This is set to change now with legislation and regulation prescribing such evaluations for listed and even large unlisted public companies.

The third major initiative, namely corporate social responsibility, that I mentioned earlier, is the focus of this conference. The topic chosen for panel discussion is "Moving Ahead with Corporate Social Responsibility", a topic of increasing interest among policymakers. How has corporate social responsibility evolved over time in India, what has been the corporate experience after CSR has become mandatory, are there any implementation issues, what is the road ahead for CSR in India, these are some of the questions that would be discussed.

The other highlight of the conference will be keynote speech which will delivered by Professor Krishnamurthy Subramanian of Indian School of Business. Professor Krishnamurthy who was also a member of P. J. Nayak Committee on governance of bank boards, will focus on governance issues in the Indian banking sector in his speech. I am sure you will find it interesting.

On behalf of NSE, once again, I welcome you all to the conference. I am sure that the deliberations of this conference would be useful for all stakeholders and contribute to the current debate on the corporate governance. I wish the conference all the best. Thank you.

Governance Issues in the Indian Banking Sector

Dr. Krishnamurthy Subramanian, Associate Professor, Indian School of Business

Somroop Mukherjee: The next program on the agenda is the keynote speech by Professor Krishnamurthy Subramanian. He is one of the world's leading experts in banking and economic policy. His service on the RBI-constituted 'Expert Committee to Review Governance of Boards of Banks in India' has established him as one of the chief architects of banking reforms in India. He is a member of the SEBI standing committee on alternative investment policy. His public policy work also extends to other sectors, including working with the Ministry of Finance to reform food policy in India. He is a member of the board of Bandhan Bank and NIBM Pune, which is chaired by the RBI Governor. Currently, Dr. Subramanian is an Associate Professor of Finance at the Indian School of Business, Hyderabad. He is an IIT graduate and has a gold medal from IIM Calcutta and a PhD from the University of Chicago, Booth School of Business. His research in banking, law and finance, innovation and economic growth and corporate governance has been published in the world's leading journals. Let me now invite Professor Subramanian to deliver the keynote speech.

Good evening, ladies and gentlemen, esteemed guests, the MD and CEO in-charge of NSE, Mr. Ravichandran, fellow panelists and friends. I think it is quite opportune that we are going to talk about governance and I am going to actually focus on the banking sector. Let me set the agenda for what I am going to talk about. I am sure you would have read in the newspapers this week and last week about how the Chairman of the Bank Boards' Bureau has written to the government about the need for steps in removing some of the stress in the banking sector. A couple of weeks back, Dr. Viral Acharya also spoke about the need for removing stress in the banking system. What I am going to talk about today is actually based on my joint work with him.

What I am going to focus on is the stress in the banking system. A lot of work that I will present here was done as part of the P. J. Nayak Committee and the follow-up work we have done. So, the lens that I am going to bring in--and which is why I think this is quite apt, given that the conference is on corporate governance--is the governance angle on banks.

I want to begin by showing you a picture (See above) of something that happened some years back. Let me give you some information and hope that you might be able to guess what was going on. The people you see in the picture are depositors standing outside a bank branch. There were several other instances of the depositors of the same bank standing and queuing up outside several branches. I would like you to guess which bank this might have been….. This bank by the way is Global Trust Bank (GTB), which as all of you know went belly-up (bankrupt) some years back. The entire sequence of events which eventually led to Global Trust Bank being bankrupt started with injudicious lending to small and medium enterprises in 1997-98. I want you to make a note of it because I will draw a parallel to something that has happened more recently and then do a 'compare and contrast', which will then lead me to some of the main hypothesis that I shall present in today's address. So, it started with injudicious lending by GTB which fuelled the Ketan Parekh led stock market scam in 2001. The magnitude of such loans by GTB was about Rs. 800 crores at that time. This actually translates to about Rs. 2,500 crores today, if you adjust for inflation. RBI inspection in 2001-02 found that the net worth of this bank was negative, which means that the value of the assets were lower than the value of the liabilities of the bank. The bank's management and the auditors claimed at that time that the net worth was Rs. 400 crores, while the RBI inspection found that the net worth was negative. RBI removed the bank's auditors, asked the Chairman to step down and lodged a formal complaint about the auditor to the Institute of Chartered Accountants of India (ICAI). And then, of course we know what happened. The picture I showed captures a run on a bank where depositors are waiting to get money, but as you can see the doors are closed and the depositors cannot get their money.

Now, let me take you through what has happened more recently, which is actually quite important. Many of you may not even have noticed. A similar story unfolded with one key difference in 2014: United Bank of India (UBI) reported a net loss of Rs. 1,238 crores in 2013-14, with more than Rs. 1,200 crores for the quarter ended 31st December 2014. It had reported a profit of Rs. 42.2 crores one year previously. Hidden NPAs were unearthed by special audits that were conducted on the instruction of the RBI. Between July and December 2014, United Bank's bad loans had jumped by over Rs. 4,500 crores. Compared to Rs. 2,500 crores in today's money for GTB, we are actually talking about almost double the amount here. UBI provided Rs. 2,260 crores to cover the NPAs and suspended all lending. Not surprisingly, the bank's union asked for a bailout from the government. The Financial Services Secretary at that time said that the government would consider a capital infusion into the bank. Recently, the government provided Rs. 810 crores of taxpayers' money to UBI.

Now did any of you notice anything like the queues I showed in the picture outside an UBI branch? None of us noticed anything. In fact, many of us may not have even noticed that there were any tremors within UBI. Business there seemed to be continuing as usual. Similar story to GTB with respect to reckless lending, mounting losses, except there was no run on UBI. And that is a key point, which I will further emphasize by giving you one more example. There was no run on Syndicate Bank either after the CBI arrested the CMD; but there was a run on GTB. The 2013-14 (relative) stress in the PSBs is at least of the same order of magnitude as GTB in 2001-02, if not more, but business continues as usual. However, in case of Global Trust Bank, there was a run and the bank had to close down. This is essentially at the heart of what I am going to talk about.

On the one hand, many of us may think that this is good. Why would you want any tremors? Why would you want a run on a bank? That is not a good thing. So, these people would argue that the government actually gives a very strong guarantee to the depositors in the PSBs is a very good phenomenon. However, that is one side of the story. The other side of the story is essentially what I am going to talk about, and I am going to give you an apocryphal story. I was not born with a silver spoon, but suppose I was born with a silver spoon: not from my dad's side but may be my uncle who was really rich. What if he told me, in a typical Bollywood style: "Ja beta aish kar" which means "go kid, have fun in life; do what you want. I am there to bankroll your fun; you can do whatever you want". What will I do? I'd basically go and not care about whether I am getting into bad company, whether I am actually doing the right things or not. I would just go and splurge and not worry about the choices that I am making in life, because I have someone to bankroll me all the time. If I go and actually run up let's say a few lakh rupees of credit card debt, it will not be a big deal. I will go and ask the rich uncle for money and he will pay up for all the losses that I have incurred. My net worth will again go positive. And then again when I come asking for money with a begging bowl, of course my uncle would box my ears a little bit and say that "next time, better take care, do not do the same things that brought you to this problem". So I say, "Of course I will be very careful" and then I go and do the same thing again, the story repeats over and over again.

So what happens is, because I have a rich uncle I will never go bankrupt – this is the positive side of things. Much like UBI or Syndicate bank never facing any tremors. But the negative side, which often times one does not get to see, is the moral hazard it creates. The fact that my behaviour is altered and I am not as careful, that is the key aspect of the story of PSBs.

So, one of the things that we did when we were working on the P. J. Nayak Committee was to look into the minutes of the latest board meeting of banks. The Reserve Bank was very supportive and had asked each of the banks to share with us the minutes of their respective (most recent) board meetings. The banks themselves were very co-operative. Now, I am sure all of you here would appreciate that the most important governance vehicle in a corporation is the board. The board is supposed to set strategy and be aware of risks. What we did was, for about a month we pored over those minutes. My team of research associates back in ISB and I read the entire set of board minutes and the agenda papers that were accompanying those board minutes. Next, we came up with a classification of issues discussed by bank boards. We classified them into issues pertaining to (a) business strategy, (b) risk, (c) financial reporting, (d) regulation and compliance; and (e) human resources. So we classified the issues that the bank boards were debating, tabling and deliberating in these five categories. What was really revealing to us was the significantly low percentage of issues that were tabled at PSB boards relating to business strategy and risk.

Now here again I will actually give you a parallel. Think about a car; the accelerator and the brake are the two most important parts in a car. Similarly in a bank, business strategy is the accelerator which delivers growth and risk acts as the brake. If you actually go headlong, just floor the accelerator without worrying about the brake, you are going to have a crash. So, both business strategy and risk are equally important. What we found was that the percentage of issues that were tabled relating to regulation and compliance was almost 45%, the issues relating to risk less than 10% and the issues relating to business strategy about 12% to 13%.

Significantly, there was an important divide between public sector banks and private sector banks. So, one of the things that stood out when we read the minutes and the agenda papers of a private sector bank is related to the analysis of risk. Let's say the private sector bank lends to firms in cement sector, textile sector, mining sector and many others. Now, the private sector bank comes under difficulty when the cement sector is not doing very well, because if the cement sector is not doing very well, the firms in the cement sector that have borrowed from it will not be able to repay the loans. Whenever a borrower borrows a loan, the bank is concerned about the borrower's ability to pay as well as willingness to pay. Let's presume for now that there is no difference in the willingness to pay, I am only talking about the ability to pay. Now, as an aside, actually it is important to keep in mind that the willingness to pay is very important and has been the elephant in the room, as we have in this country several companies that are bankrupt, but their promoters are very rich. But, be that as it may, if suppose the cement sector is not doing very well, the ability to pay of companies in the cement sector will certainly go down. And therefore, what one finds is that the private sector bank starts experiencing stress in the loans that it had disbursed to the cement sector.

Now, if you take a public sector bank, what you would find is a perfunctory analysis. "Our exposure to the cement sector has been 25% so far; should we increase it or decrease it?" Okay maybe increase 2% or decrease 2% and that is the end of the story. In contrast, if you read notes of the agenda papers and the board minutes of the private sector bank, what you would find is a very deep analysis of the prospects of the cement sector. In other words, how is the cement sector going to look one year from now, two years from now, three years from now, which then affects the performance of the loans that have been given to cement companies this year. In other words, and this is something which I teach my students, risk is always a forward-looking matter, risk is not backward looking. You gaze into a crystal ball and ask yourself, "What will be the prospect of the company that I have lent to one year from now, two years from now, three years from now". So, you basically find the private sector bank asking that forward looking question and this is just one example. Though this is not generally true, i.e. not all private sector banks do a forward-looking analysis of the risks that their loans are exposed to, some private sector banks are undertaking a very careful analysis of risk. It is not a perfunctory analysis as it certainly is in the case of public sector banks.

Similarly, if you pick up the minutes of the risk management committee and study how much time is spent, how many words, how many sentences, how many paragraphs, issues relating to risk are being actually tabled, it turns out that private sector banks are doing better than public sector banks that are not doing much at all. We used sophisticated tools like text mining to try and find out how many words, sentences, paragraphs etc. and contrasted the minutes of the private sector bank I referred to before with all public sector banks. Now, this is essentially an aspect of governance and unless one makes that extra effort to explore what is really happening, one would not realize that it is actually a governance problem. It goes back to that apocryphal example that I gave you. If I have a rich uncle who is willing to bankroll me every time I run into problems, I have no incentive to actually really dig deep into my own reserves, talent/ability and try to do my best in terms of choices.

This is the key moral hazard that we actually face in public sector banks. I was looking at some numbers for recapitalisation in PSBs: Rs. 70,000 crores has been allocated for capital infusion into public sector banks in the next five years by this government after it came into power. By the way, that may be a story for later where we would talk about what brought us to this path. Now, just make a comparison of this government spending to anything else. You will find that it is of a similar order of magnitude to our defence spending, spending on healthcare, spending on education. As an economist I actually understand the concept of opportunity cost; if the Rs. 70,000 crores were not put into these public sector banks, which actually seem like a bottomless pit, then the Rs. 70,000 crores could have been used for funding education of our young children, funding the health of our population and in many other ways. These are by the way questions that we as citizens and the CAG should be asking.

So what I want to focus on is the issue of governance. The fact is that there is significant moral hazard, as a result of which you have public sector banks in deep distress. There are two key aspects to how this governance problem shapes up. First, the government has majority ownership (more than 50%) in public sector banks and that by the way brings up another key issue which is minority shareholder expropriation. If I recall correctly, the market to book value ratio of many of the public sector banks is less than one. In contrast, the same ratio for a private bank such as Kotak Mahindra would be more than 6. This means that every rupee that has been invested in the balance sheet of Kotak Mahindra is worth six times on the stock market. Imagine the value that the minority shareholder is reaping by investing in Kotak Mahindra Bank versus the value that a minority shareholder is reaping when he or she invests in the public sector banks, because the Re. 1 that is invested by a shareholder of a public sector bank is not even worth that Re. 1. But, this is only a symptom. If the fact that the market to book is so low for PSBs is a symptom, what is the cause? The cause is the governance.

I want to give you some more color on the governance. There are two key aspects of how governance gets abused. One is about the selection of people on the public sector bank boards. We were really privileged in the Nayak Committee to have two former chairmen from the public sector banks who shared their experiences about how they had to "manage the board". While the board is supposed to actually help the CEO build strategy, make sure there is an understanding of risk and so on, some members of the board were driven by their personal agenda.

Now, is the blame to lie with the director who is doing this or the one who is selecting such directors? I will again use an example to just drive home the point. Suppose for a test match to be played by the Indian team, we go and get some ordinary player from a Ranji Trophy Team to play, what will happen? It is likely that out of the 11 places one place is taken by someone who is not worth it, who does not contribute and the team will not perform very well. The blame will be laid on whose doorstep? It is the person who is actually doing the selection. The point I am making is that the way the selection process for board members in public sector banks is undertaken is severely flawed.

Here it is important to note that world over, selection of people at the topmost level is always done by peers. As an example, I am sure that the CEO of the National Stock Exchange was not selected by some politician or some bureaucrat. It was actually selected by the Board of NSE through a formal search process that involved people who knew what it takes to actually run National Stock Exchange. Similarly, if it is any of those private sector banks, the people on the board are selected by other people on the board. It is the Nomination and Remuneration Committee (NRC) of the Board that does this. So, for instance in Bandhan Bank, if I as a board member do not contribute to the discussions in the board meetings, the NRC basically will bid me goodbye at the end of my tenure. However, if I am doing my job well I will get appointed again. Through our research we found that the boards of PSBs are actually set by law: the Banking Regulation Act and the Bank Nationalization Act. In fact, the Bank Nationalization Act, in particular, specifies who can be on the boards of Banks. This is different from corporations that are governed under the Companies Act, where board composition is decided by the firm. By the way, banks are not corporations under the new Company Law because they are just legally designated entities created by the Bank Nationalization Act. As a result of this codified in the law (through the Bank Nationalization Act), there has to be a Chartered Accountant (CA) on the board. And it turns out that almost 90% of the Chartered Accountants on the public sector bank boards are from Mumbai and Delhi. Now, I think it is anybody's guess that not all the talent among Chartered Accountants is concentrated in Delhi and Mumbai. Kolkata, for example, has a lot of excellent Chartered Accountants and yet, Kolkata does not have enough representation in bank boards. Why? Because people who are in Kolkata are perhaps not so close to the powers that be, the political connection is not there and these CAs do not get to go on the boards. This is one way of how the process of appointment of directors on the boards of public sector banks is politicized.

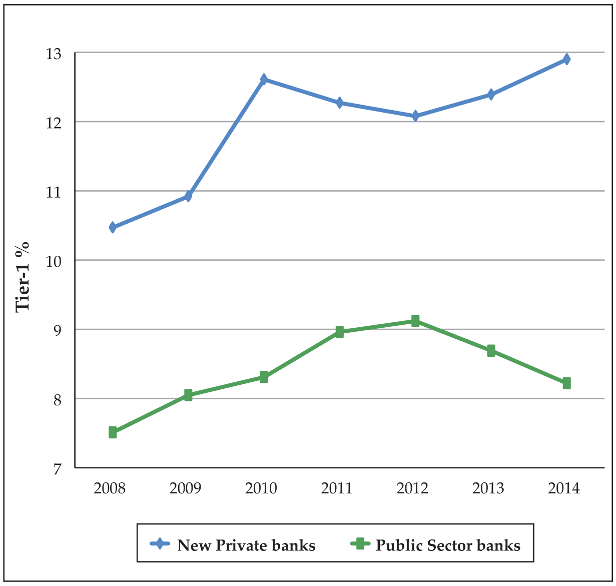
Let me now talk about the second aspect of governance, which relates to the bureaucrats. Banking is a very complex activity. Before I joined the Bandhan Bank board, my experience with a bank was that of a customer, either to withdraw money from the ATM or may be actually talk to the teller or the branch manager. I had worked with ICICI Bank in junior positions for two years but that is completely different from actually running a bank. Now, if I am asked to actually run a bank, I would not know what it takes because I do not have that knowledge. Similarly, bureaucrats who have only stepped into banks as customers are telling the public sector bank chairman what to do. And this is again based on data. What we did was, from 2001 we picked up all the circulars that were issued by the Ministry of Finance to the public sector banks. We found that right from ALM (Asset Liability Management) to the way the software must be deployed in public sector banks, the bureaucrats micromanage everything through these circulars. And these are people who have themselves never ever worked in a bank; nor do they have any expertise in banking. This is one other aspect of the problem, on which I had written a piece in The Economic Times. So, a bureaucrat who has never stepped into a bank is telling a public sector bank chairman who has spent 35 to 40 years in the banking business how he should be running the bank. It is like me telling Virat Kohli how he should be running the Indian cricket team. What cricketing expertise do I have to tell Virat Kohli how he should be running the Indian cricket team? And yet, this is what happens with bureaucratic interference in PSBs. Add to this the politicization during the previous regimes, the phone calls that came asking chairmen to give a loan to 'X' or 'Y' and the like. Then, you have the ultimate explosive combination that we are witnessing now. Not surprisingly, several loans to infrastructure sector and some other sectors are really under stress.

The ultimate result of this aspect of bank governance is that the public sector banks are thinly capitalized. In fact, our numbers show that in the next few years anywhere between approx. Rs. 3.5 trillion to Rs. 7-8 trillion of capital will be required by the public sector banks. So, Rs. 70,000 crore is basically just peanuts, or as they say in Hindi, "Unth ke muh me jeera". Thus, they (the PSBs) are really undercapitalized. The only way in which the government can actually provide that much amount of capital is by slipping on its fiscal deficit targets.

We did different scenarios for banks' capital requirements. In Chart I below, the green line plots those banks that are really impaired. Several of the public sector banks are impaired even in the least conservative scenario (Scenario 3); that is, they do not have the capital that is required by the regulator. If you look at the private sector banks though, they are actually very well capitalized.

Overall, as a percentage of their market capitalization, the amount of capital required is significantly higher for the public sector banks than their private counterparts (Table I). One option to actually raise this capital could be to sell the stakes of the public sector banks. The government owns more than 50% in PSBs. So, what the government can do is to come down to 52% or maybe 50% so that it holds majority ownership and yet raises capital. At the kind of valuations that are prevailing right now, the maximum amount that can be raised will be about Rs. 45,000 crores to Rs. 50,000 crores (Table I). It is nowhere close to what is required by the public sector banks to meet the Basel III norms. This is the other important aspect.

Chart I: PSBs are thinly capitalized compared to their private counterparts



Bank Name	Tier-1 CAR	Impaired Tier-1 CAR (Scenario 1)	Impaired Tier-1 CAR (Scenario 2)	Impaired Tier-1 CAR (Scenario 3)
Public sector banks				
STATE BANK OF INDIA	9.72	4.09	7.36	9.10
ALLAHABAD BANK	7.51	0.32	4.31	5.86
ANDHRA BANK	8.09	(0.10)	4.49	6.18
BANK OF BARODA	9.28	4.72	7.87	8.90
BANK OF INDIA	7.24	3.79	5.70	6.52
BANK OF MAHARASHTRA	7.44	3.54	6.35	7.30
CANARA BANK	7.68	2.46	5.63	6.44
CENTRAL BANK OF INDIA	7.37	(3.15)	2.73	4.57
CORPORATION BANK	8.14	0.90	5.02	6.32
DENA BANK	7.43	2.09	5.54	6.54
IDBI BANK LIMITED	7.79	4.05	6.40	7.36
INDIAN BANK	10.24	4.59	7.87	8.97
INDIAN OVERSEAS BANK	7.47	1.86	4.87	6.10
ORIENTAL BANK OF COMMERCE	8.86	0.10	5.25	6.66
PUNJAB AND SIND BANK	7.62	(0.29)	4.20	5.56
PUNJAB NATIONAL BANK	8.87	2.00	6.16	7.64
SYNDICATE BANK	8.68	3.08	6.83	8.00
UCO BANK	8.71	2.71	6.87	8.44
UNION BANK OF INDIA	7.54	2.66	5.55	6.71
UNITED BANK OF INDIA	6.54	(1.46)	2.16	4.39
VIJAYA BANK	8.12	4.14	6.69	7.57
Private sector banks				
AXIS BANK	12.62	12.60	13.86	14.22
DCB BANK LIMITED	12.86	14.21	14.55	14.55
HDFC BANK	11.77	14.01	14.07	14.07
ICICI BANK	12.78	12.75	13.83	14.34
INDUSIND BANK	12.71	14.58	14.69	14.69
KOTAK MAHINDRA BANK LTD.	17.77	19.48	19.56	19.88
YES BANK LTD.	9.80	12.00	12.03	12.03

Table I: Capital shortfall in PSBs and possible proceeds from stake sale

	Capital shortfall ('000 crores)			Capital shortfall as a multiple of total equity market capitalization (as of 7-May-2016)		
	Scenario 1	Scenario 2	Scenario 3	Scenario 1	Scenario 2	Scenario 3
Allahabad Bank	28.3	18.4	14.4	5.0	3.3	2.5
Andhra Bank	17.5	10.8	8.0	4.1	2.5	1.9
Bank of Baroda	57.3	32.9	22.9	1.7	1.0	0.7
Bank of India	83.4	57.4	46.8	6.2	4.3	3.5
Bank of Maharashtra	21.8	15.5	13.0	5.7	4.1	3.4
Canara Bank	78.0	53.7	43.8	4.6	3.2	2.6
Central Bank of India	45.7	32.3	26.8	2.5	1.8	1.5
Corporation Bank of India	21.3	13.5	10.3	4.6	2.9	2.2
Dena Bank	18.2	12.1	9.7	6.7	4.5	3.6
IDBI Bank	63.2	44.1	36.3	5.8	4.0	3.3
Indian Bank	20.9	12.4	8.9	3.0	1.8	1.3
Indian Overseas Bank	47.2	33.6	28.0	9.3	6.6	5.5
Oriental Bank of Commerce	28.8	19.3	15.4	5.1	3.4	2.7
Punjab & Sind Bank	13.5	9.4	7.7	7.1	4.9	4.0
Syndicate Bank	59.9	34.4	24.0	2.1	1.2	0.8
UCO Bank	264.2	166.8	126.9	1.3	0.8	0.6
Union Bank of India	23.4	14.8	11.3	3.6	2.3	1.7
United Bank of India	22.2	14.1	10.8	3.5	2.2	1.7
Vijaya Bank	47.0	31.6	25.3	5.6	3.8	3.0
United	21.5	16.4	14.3	9.3	7.1	6.2
Vijaya	14.2	9.6	7.7	3.7	2.5	2.0
Total	**997.4**	**653.3**	**512.3**	**2.6**	**1.7**	**1.3**
Min	**13.5**	**9.4**	**7.7**	**1.3**	**0.8**	**0.6**
Max	**264.2**	**166.8**	**126.9**	**9.3**	**7.1**	**6.2**
Average	**47.5**	**31.1**	**24.4**	**4.8**	**3.2**	**2.6**

Bank Name	Govt stake (%)	Mkt Cap (May 7) in '000 crores	Max stake sale (%)	Proceeds from stake sale based on mkt cap on May 7 in '000 crores
Allahabad Bank	58.9	5.7	6.9	0.4
Andhra Bank	60.1	4.3	8.1	0.3
Bank of Baroda	56.3	34.0	4.3	1.5
Bank of India	66.7	13.4	14.7	2.0
Bank of Maharashtra	85.2	3.8	33.2	1.3
Canara Bank	69.0	16.9	17.0	2.9
Central Bank of India	88.6	18.1	36.6	6.6
Corporation Bank	63.3	4.7	11.3	0.5
Dena Bank	58.0	2.7	6.0	0.2
IDBI Bank	76.5	10.9	24.5	2.7
Indian Bank	81.5	6.9	29.5	2.0
Indian Overseas Bank	73.8	5.1	21.8	1.1
Oriental Bank of Commerce	59.1	5.7	7.1	0.4
Punjab National Bank	58.9	29.0	6.9	2.0
Punjab And Sind Bank	81.4	1.9	29.4	0.6
SBI	58.6	197.7	6.6	13.0
Syndicate Bank	67.4	6.5	15.4	1.0
UCO Bank	77.2	6.3	25.2	1.6
Union Bank Of India	60.1	8.4	8.1	0.7
United Bank Of India	88.0	2.3	36.0	0.8
Vijaya Bank	74.1	3.8	22.1	0.8
	Total			**42.4**

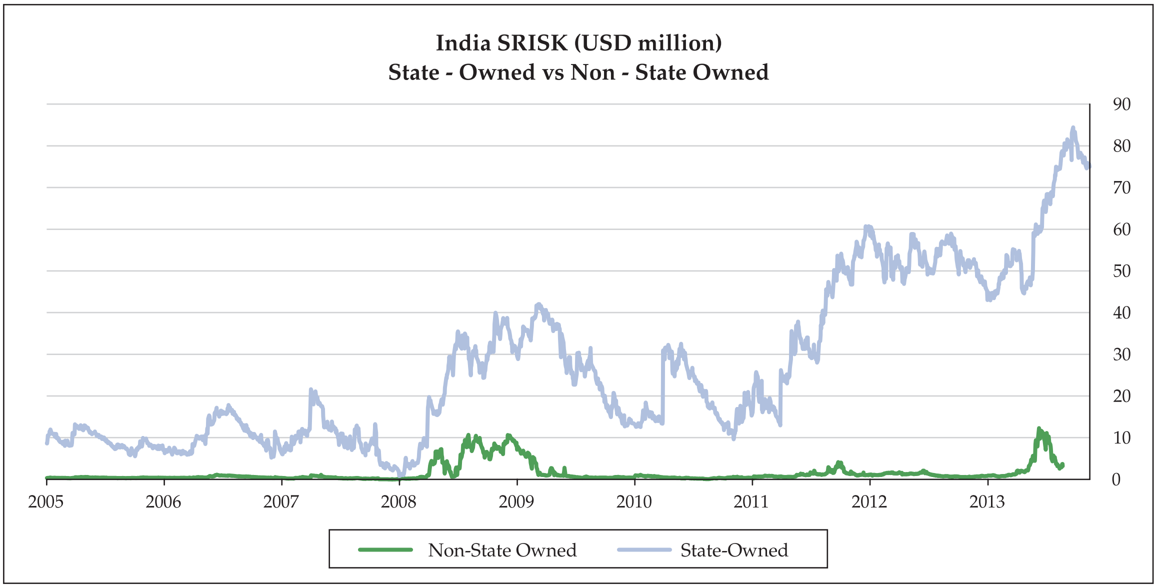
So, whenever the government needs to infuse capital in the public sector banks and cannot do it directly, it reportedly persuades the LIC (Life Insurance Corporation of India) to do so (Table II), and this does not get categorized as government's capital infusion because LIC is basically seen as another investor. But LIC is essentially an arm of the Government of India and according to the LIC Act, there is an explicit guarantee that is given by the government to LIC, which means that if any person is going to lose deposits or the insurance money in LIC, the government will actually backfill it. So, what happens if the market value of these investments by LIC in the public sector banks crash? LIC starts coming under distress. If LIC comes under distress, the government starts coming under distress. How? Imagine the following, a small car, say Nano falls from a cliff. To lift the Nano let's say you get a Honda City. While trying to lift the Nano, the Honda City falls down. Then in order to actually lift the Honda City and the Nano you actually summon a truck. In trying to lift both the cars, the truck also falls down. This is exactly what will happen. Nano is actually public sector banks, Honda City is the LIC and the truck is the Government of India. If LIC comes under distress, the government will certainly come under significant distress as well.

Table II: LIC stake in PSBs

Bank name	Sep-13	Sep-14
Corporation Bank	24.69	22.54
Indian Overseas Bank	8.91	14.23
United Bank	4.60	14.19
SBI	13.43	13.50
Bank of Maharashtra	7.82	13.41
Dena Bank	5.92	13.12
Bank of India	12.67	11.81
Punjab National Bank	13.15	11.78
Bank of Baroda	12.01	10.57
Punjab & Sind Bank	4.56	10.49
Central Bank	7.03	10.04
Allahabad Bank	10.76	9.94
Union Bank	10.85	8.78
Oriental Bank	10.61	8.22
Syndicate Bank	11.03	8.18
UCO Bank	10.20	7.91
IDBI Bank	8.63	7.00
Andhra Bank	7.98	6.74
Canara Bank	5.48	6.04
Vijaya Bank	12.09	6.00
Indian Bank	2.42	2.60
State Bank of Bikaner	2.22	2.02
State Bank of Mysore	1.47	1.47

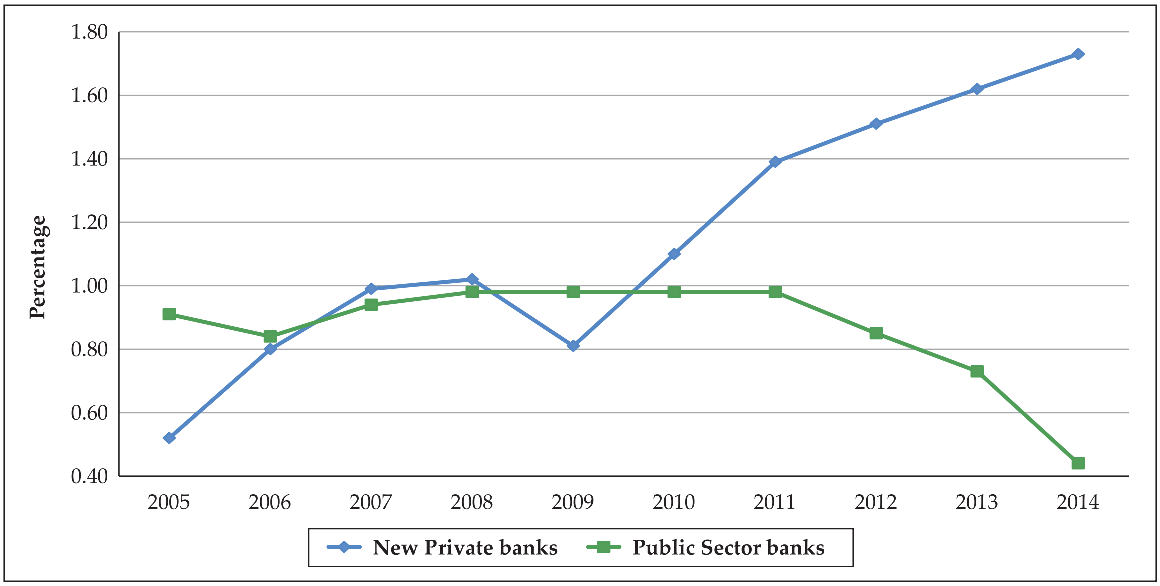
So, this is the other aspect of how systemically risky the public sector banks are. We know from what happened in the financial crises. After Lehman Brothers failed a lot of the banks came under significant distress. Why? Because these banks had counterparty exposures to Lehman Brothers. Similarly, tomorrow if any of the public sector banks comes under distress, because of their counterparty exposures to the other public sector banks and the private sector banks, the risk in all banks will rise. Chart II below gives you a measure of systemic risk in public and private sector banks. The green line refers to the private sector banks and the grey line to the public sector banks. The systemic risk in the private sector banks has not increased that much but in the public sector banks it has increased significantly. So on the one hand, you have thinly capitalized public sector banks who have become a lot more systemically risky, and there is more coming.

Chart II: PSBs are incredibly systemically risky



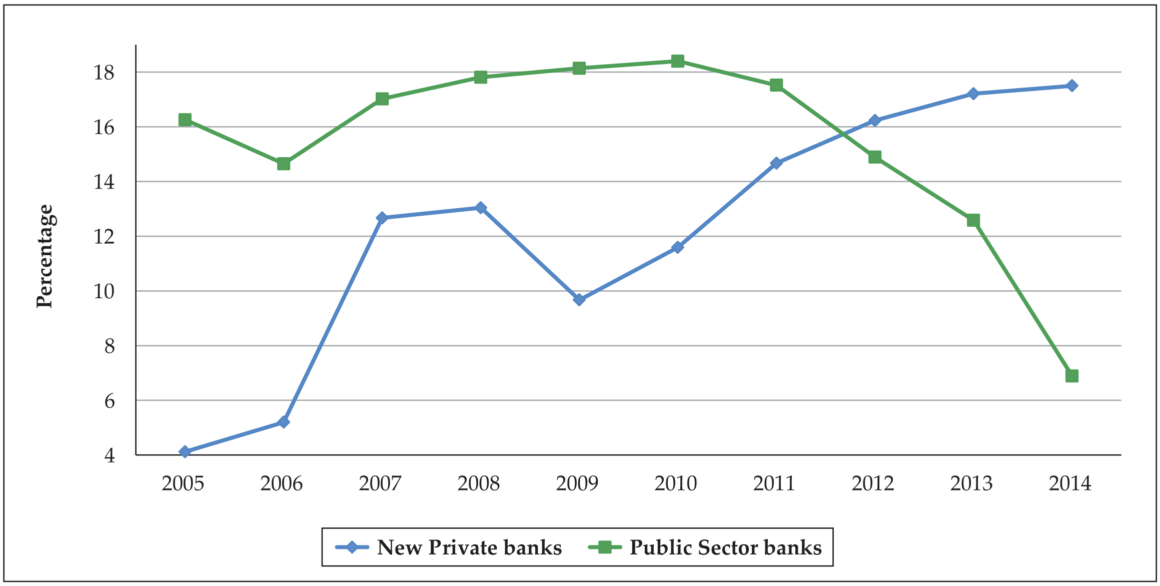
Now let us look at the return on assets (Chart III). The green line refers to the public sector banks while the blue line to the private sector banks. This is a plot from 2005 to 2014, so till about 2008 things were very good. Why? Because the economy was doing very well. Some commentators say that there is no need for a change in the governance in public sector banks; these banks were doing really well up till 2008 - 2009. Fair point. But, what you have to remember is that governance problems come under the spotlight only when firms start doing poorly. It is like only when the tide goes away that people come to know who has been swimming naked. So, governance problems come to light only when things are not happening very well. Of course, up until 2008-2009, the public sector banks were doing well, but what you find subsequently is a precipitous fall. It is a scissor-like movement where the private sector banks' return on assets has been increasing while the return on assets for the public sector banks has fallen sharply.

Chart III: Return on assets



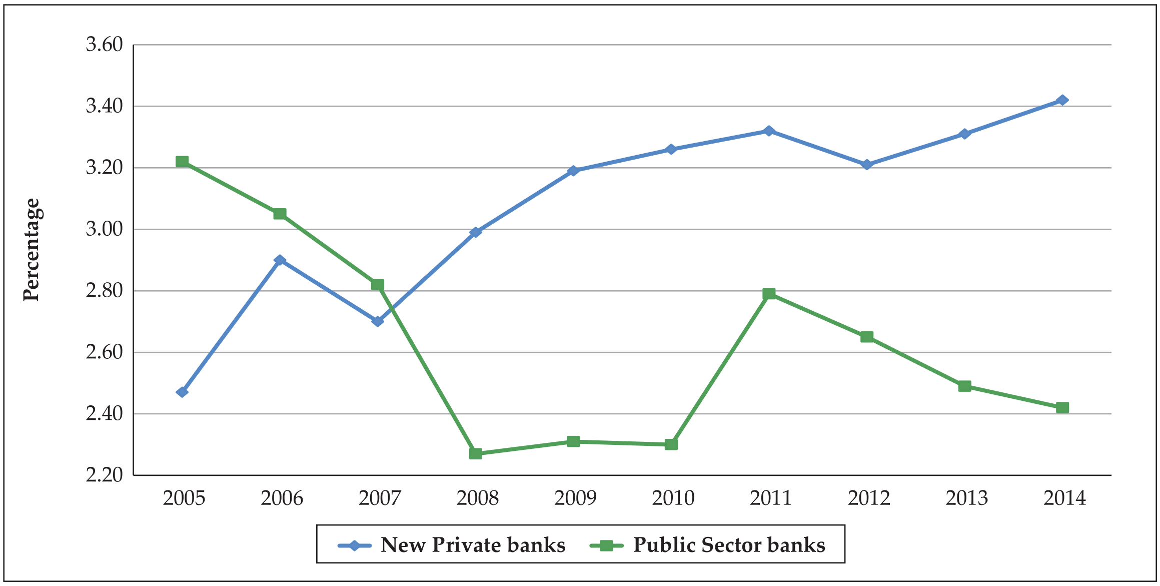
Similar is the case with return on equity (Chart IV). Banks are heavily leveraged. So if you take an Indian corporation, which has two units of debt for every unit of equity, you would call that very highly levered, even though typical Indian corporates now are significantly leveraged. But banks often carry multiples of that. So if a bank has 10% equity capital, that is considered to be excellent. This means for every unit of equity there are nine units of debt in the capital structure. So, now you can certainly appreciate that even a small shock can actually take banks down because the debt in their capital structure is significant. That is essentially what you find in Chart IV; the difference in return on equity between public and private sector banks has reversed from being positive to negative with the return on equity falling significantly for PSBs from 2010 onwards.

Chart IV: Return on equity



Look at the net interest margin (Chart V). This is basically the difference between the interest rate that banks earn on loans and the interest rates that they pay on deposits. So, this is a measure of a banks' profitability. Here again, the public sector banks have been doing really poorly and a lot of the stress started actually in and about 2008 or so.

Chart V: Net Interest Margin



Net non-performing assets is something that everybody knows about (Chart VI). Actually there has been an exponential increase in the non-performing assets. If we exclude the restructured assets and just talk about the stressed assets, you see the same picture. Asset growth has been actually high. The problem has been that asset growth (Chart VII) has happened without adequate prudence in the lending.

To summarize, what has ailed the public sector banks is really its weak governance resulting in the ills that are affecting them, some of which I spoke about. The onus of correcting this situation actually lies with the Government through radical reforms. I do not know how many of you actually had a chance to read the piece I wrote in the Economic Times after the last budget. My main submission was that nothing has been done for the banking sector; all the problems that were there before the budget have continued. There has been nothing done to take care of these problems. In fact, the 'Indradhanush' set of reforms the government had announced in August of last year have hardly been initiated.

Chart VI: Net non-performing assets

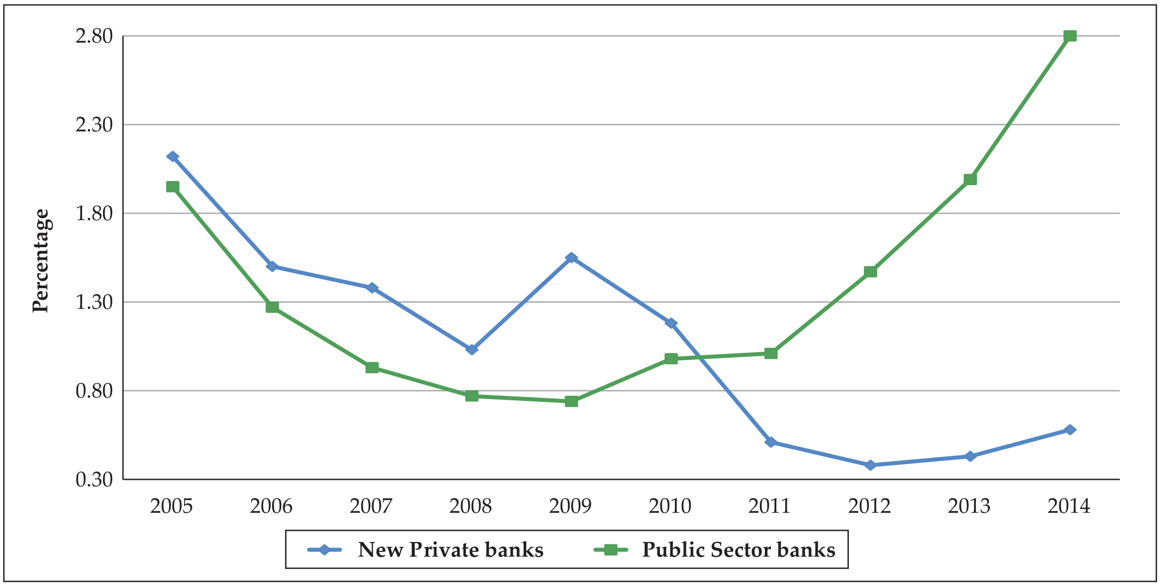
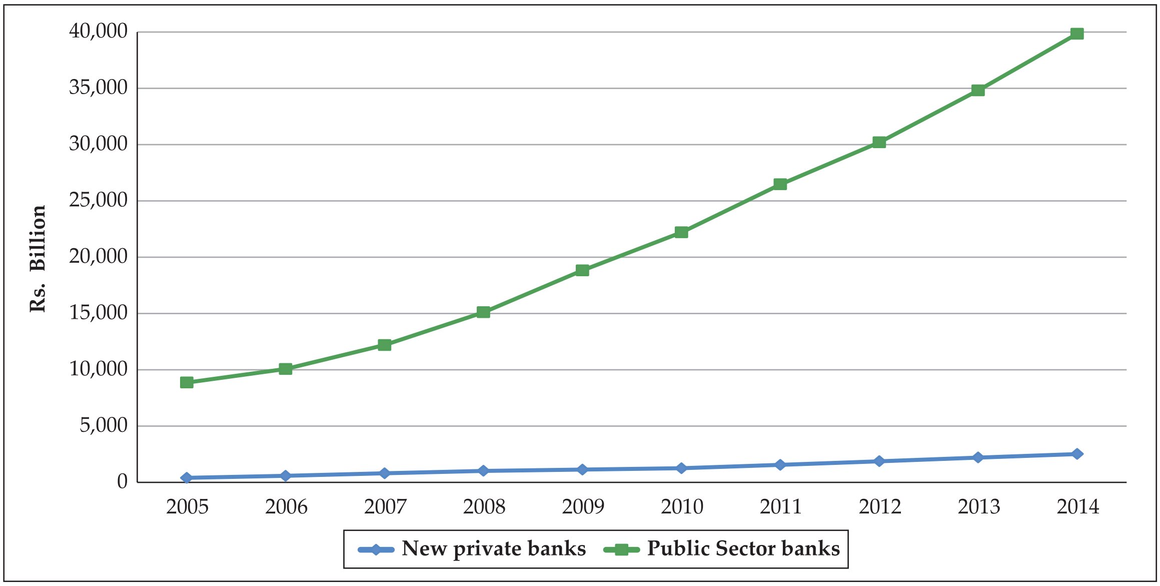


Chart VII: Growth in Asset-size



In addition to creating a Bank Board Bureau, one of the main recommendations that we had made in the Nayak Committee was to cut the umbilical cord that connects the government to the public sector banks, not by necessarily reducing the government's stake but by creating a holding company. The holding company is basically what would be responsible for the governance. This was something that was mentioned in the previous budget speech but there has been very little action on that. So, unless that umbilical cord is cut, the governance problems that we have talked about will not go away. We will have these periodic episodes of distress and the profligate son going to the uncle with a begging bowl asking for money. That is what will continue.

So, absent such reform or with piecemeal reform, it is unlikely that there will be material improvement in the performance of public sector banks. This could impede the government's objective of fiscal consolidation, as I mentioned, in terms of the numbers that we are looking at. If the government decides not to spend 'taxpayers' money in such recapitalization, the public sector banks will have to shrink their balance sheets significantly. So, there are two ways of actually getting out of this mess. One is that if you need to grow your assets you require the capital. But if the capital is going to stay at the current level, the asset size has to shrink. So as a result, what you will find is that the public sector banking space will shrink significantly as we go along, which may have significant effects on economic growth.

I want to leave you with this final thought that double-digit economic growth cannot happen with an anaemic banking sector because, in this country and a lot of other economies as well, the banking sector is basically the heart of the body. If the body has to be vital, a clogged heart cannot actually deliver the flow; which is basically the flow of credit. You cannot get that double-digit or even close to double-digit growth with the banking sector being as anaemic. And the only way that these clogged arteries can actually be healed is not by putting band aid on left side of the body but by actually doing a bypass surgery.

Happy to take questions.

Participant: Do you see vigilance or excessive vigilance being a very important factor in risk aversion?

Krishnamurthy Subramanian: Excellent question. In fact, I would have loved to touch on that more. I am glad that you raised this question. What you said is certainly true. But, more importantly, it also has important implications for why we are not able to resolve the distress in the banking system. World over when loans are in distress, banks have to do debt restructuring, and in debt restructuring banks often have to settle for less. Suppose, there is Rs. 5,000 crore of money that is owed, let's say, by company X. The bank may have to settle for Rs. 4,000 crore to actually restructure. But imagine what will happen actually if I am the public sector bank chairman who is willing to take Rs. 4,000 crore instead of Rs. 5,000 crore. The first thing that will happen after the chairman has signed that deal is that she will get a call from CBI or from CVC saying how much money did you take from the promoter. Also, there would be allegations that the government is siding with the rich. Anticipating all these problems, no bank chairman wants to take that hard call. So, basically you end up kicking the can down the road saying okay I will not deal with it. Let the next chairman do it. The next chairman passes the baton on to the next chairman and so on.

Participant: How much stress is caused by promoter intervention in the management of public sector banks? In this case, promoter is the government.

Krishnamurthy Subramanian: Entirely.

Participant: What do we need to deal with this situation?

Krishnamurthy Subramanian: A large part of the blame will have to be laid at the hands of the promoter. Let me mention right now from what I know. This government has not been interfering in the affairs of the banks, but that may be a one-off. What you want is checks and processes, the mechanisms to be built so that even when a government wants to meddle or a bureaucrat wants to meddle, the processes and the mechanisms are such that they cannot meddle. This is actually what the Nayak Committee report has suggested and ideally, we would want that to be implemented.

Participant: You said our banking system is the heart, right? And people who are holding important positions are not having the proper knowledge.

Krishnamurthy Subramanian: Okay, let me clarify. What I meant was some of the directors that are selected. Make no mistake, the chairmen of the public sector banks and senior management are phenomenally well qualified; they know their stuff. They are very good people, no question about it. Except, much like in any pond there will be some rotten fish. Overall, it is very good. But it is those other directors on the boards of PSBs who actually are not selected through a mechanism that emphasizes merit and competence.

Participants: Why does the banking system fail? Why are there huge NPAs?

Krishnamurthy Subramanian: Because of exactly what I have spoken about. The incentive mechanisms are such that if I know very well that when I mess up somebody else will actually fill in for me, I have every incentive to actually go and mess up, even if I am the most capable manager.

Participant: Are they not questionable?

Krishnamurthy Subramanian: They are questionable. This is the main aspect that I am talking about

Participant: Continuing on your cricketing analogy, you obviously have some strong views on the problem that we see at hand. Just to end on an optimistic note, if you were deputed to be the coach for the next match in Dharamshala, what is the one thing that you would do? Is there a silver bullet to clean this up? Because we are just pushing the entire thing down the road. I mean, $10 billion for recapitalization, from where is it going to come? Even if you raise capital from the public through sale of shares, the crowding out effect comes in. So you are between a rock and a hard place. What is that one thing that you would like to do to cleanse the mess?

Krishnamurthy Subramanian: No, I would not claim I know of a silver bullet; that would be extremely ambitious. But I think we have talked about this in the Nayak Committee. Governance is what we have identified as the key issue and the solutions we have proposed are primarily to fix governance issues. The governance starts with the promoter, as someone in the audience pointed out, the government. Extending the cricketing analogy, I have here somebody who may not have the right ability and possibly does not have the right intentions as well, but, is framing strategies and telling people how to do things of which they have no idea. So, what I would fix is basically the coach of the team here. Essentially, the owner needs to actually get away from managing and directing the cricketing aspects, which he has little knowledge of. If you have let's say Deccan Chargers or any other team, the owner can invest the money and let the cricketing people actually take care of the cricket. Ask at the end as to how is my money doing; that is the owner's prerogative for sure. But the owner must not decide tomorrow that this guy should be playing the match and this guy should actually be bowling the 19^{th} over; this is something that is completely outside the owner's expertise.

Participant: Supposing the owner thinks that he is the expert, then what happens? I think that is the problem.

Krishnamurthy Subramanian: I read somewhere that a genius is someone who knows that he is a fool, Reverse it, a fool who does not know that he is a fool actually is the biggest fool.

Participant: I have a question. what similarities and differences do you see between India and China? Because China also has a big state owned banking sector.

Krishnamurthy Subramanian: I think there are a lot of similarities. In fact, the Chinese banking system is also under a lot of distress. The one big problem though we have with China is, we actually have no idea how bad it is because transparent data that you can trust is actually very hard to come by. But from talking to other experts on baking sector who work on China, Japan etc., I believe that the Chinese banking system is also under a lot of stress, precisely because of some of the governance problems.

Participant: I was surprised that you did not name the holding company that you have suggested in the Nayak Committee, as a silver bullet. From your speech, I thought this is how it was emerging. RBI had put out a paper, which it quickly deleted from its website on this holding company several years ago, I think in 2007 - 2008. What I meant is, there must be some political economy related questions there. Did you try to see what those were?

Krishnamurthy Subramanian: I must admit that in 2007-08, I used to be in the US, not following this particular aspect, so I am not aware of the holding company idea being mooted in 2007-08. And even during our discussions with the then RBI Governor, Dr. Rajan, this was not brought to our knowledge. I did not want to call the holding company a silver bullet but that is a solution we have in mind. A lot of thought has been put into the proposal for the holding company. Basically, if you go and read the relevant chapters, you will see that we have actually brought in evidence from Singapore, for instance Temasek. Basically, the structure is similar where the Singapore Government, through a holding company, has holdings in Temasek. Also, in Brazil, South Africa and a number of other emerging economies, where you see governments actually being involved in the banking sector, a holding company structure has been employed. So, we would like to believe that a) the analysis that we have done is a lot better in this round, in the Nayak Committee, and b) we have thought through by giving examples and even analyzing those examples with how the holding company structure is likely to work a lot better in this report.

What framed our thought here was, if you just think conceptually, when a government is involved in a commercial enterprise it can play three roles. It can play the role of just an owner resembling, let's say, an IPL team owner who at the end of the year asks for results. Second, you could have the government playing the role of an investor. Third, the government could play the role of a sovereign doing anything and everything. Right now the government actually plays the role of the sovereign and the evidence seems to be that in whichever country the government plays the role of a sovereign in the government owned banks, such banks actually have these periodic episodes of distress and do not do very well. When the government is less involved, the country ends up having a much better banking sector as an outcome.

Thank you very much for all your questions. We will discuss remaining questions over dinner.

Moving Ahead with Corporate Social Responsibility

Dr. Jayati Sarkar, Professor, IGIDR

Somroop Mukherjee: The final session of today's program is going to be on mandatory CSR according to the Companies Act. I invite Professor Jayati Sarkar on stage to deliver the presentation on "Moving Ahead with Corporate Social Responsibility".

Good evening. On behalf of the National Stock Exchange and Indira Gandhi Institute of Development Research Corporate Governance Research Initiative, I take immense pleasure in welcoming you to this panel discussion on "Moving Ahead with Corporate Social Responsibility". The Companies Act 2013 has been a watershed legislation that has led us to rethink the role of corporation and society through Corporate Social Responsibility (CSR). With Section 135 of the Act making CSR mandatory, a large section of Indian companies have been drawn into social welfare programs in a substantive way to supplement existing government and non-governmental efforts and pull out large sections of our citizens out of poverty. With two years of implementation of mandatory CSR behind us, I think it is an opportune moment to take stock of what we have achieved, what are the governance challenges, what is the road ahead and how do we address these to make this policy successful. Hence, we have organized this panel discussion today. I am very happy to tell you that we are privileged to have amongst us distinguished panelists who are from different fields with regard to CSR. They shall be sharing their experiences and expertise on this topic. We have Mr. Santhosh Jayaram, Ms. Sanjukta Raiguru, Ms. Gayatri Subramaniam, and Ms. Shaheen Mistri. They have been making invaluable contributions to the social sector of this country in carving out the role of Indian businesses in our society through CSR.

I will start this panel discussion with a short presentation of the background note that we have prepared, just to set the stage for the panel discussion and to bring out certain issues that are likely to come up in the course of the panel discussion.

I shall now be presenting some of the results from an ongoing research which I am conducting jointly with my colleague, Professor Subrata Sarkar. I shall report the results of some of the analysis that we have undertaken. The structure of the presentation is basically an evaluation of mandatory CSR in India, along with some idea of benchmarking with what the companies were doing during the voluntary CSR period. We will then look into mandatory CSR and take stock of what has been happening in the last two years, especially with the most recent data we have analyzed for 2015-16, and finally discuss the road ahead.

For the uninitiated, there are thousands of definitions pertaining to CSR but the most commonly used definition is that CSR is essentially a multidimensional concept that can be differentiated into four inter-related components--economic, legal, ethical and philanthropic responsibilities. We are basically moving beyond just the economic objectives, and in India the definition of CSR extends beyond just the economic objectives – it is about businesses embracing the triple bottom line approach whereby its financial performance can be harmonized with the expectations of society, environment and stakeholders in a sustainable manner. The definition essentially encompasses the relationship between business and society. Another point is that in some way it redefines the goal of the corporation from the shareholder perspective to the stakeholder perspective; i.e. the corporation needs to not only meet the objectives of the shareholders but other stakeholders as well. If we go through the institutional evolution of mandatory CSR which dates back to 2009 when the government came up with the voluntary CSR guidelines, it was a way of encouraging the corporate sector to get involved in CSR activities. The essence of such activities was that it was voluntary.

Then in 2011, another document named 'National Voluntary Guidelines for Social Environment and Economic Responsibilities of Business' was introduced. Even in this case, participation in CSR activities was made voluntary. The first step towards making CSR mandatory can be traced back to 2012 when Clause 55 of listing agreement by SEBI was introduced. It mandated business responsibility reporting by top 100 listed companies. It made the disclosure of CSR expenditures (under various heads) mandatory. Finally in 2013, Section 135 of the Companies Act made CSR mandatory for a particular section of companies in the Indian corporate sector and subsequently in 2014, it was implemented. Thus, CSR in India has basically transitioned from voluntary to a mandatory regime. I think most of you know that mandatory CSR is applicable to companies which satisfy some criterions and these companies are basically required to constitute a CSR committee of at least three directors, of which, one would be independent director. The responsibility of the CSR committee is to ensure that the company spends at least 2% of the average net profits during the three immediately preceding financial years on CSR and report the amount spent.

Legal compliance is again an important point that our panelists are going to discuss. Basically, it boils down to 'comply or explain'. In case of noncompliance, i.e. if a company does not meet the mandatory CSR spending, it has to explain why it has not been able to meet the required target and to the best of my knowledge, I did not come across penalties for noncompliance. Some points to remember while evaluating mandatory CSR would be: (a) Companies are encouraged to give preference to the local areas for spending the amount earmarked, so it is sort of easier to monitor, (b) Companies are allowed to collaborate among themselves on CSR projects, so that they can pool resources, which may lead to efficiency and there is no duplication of efforts, (c) Companies can undertake CSR projects through a registered trust, society, or company, and (d) Last of all, the Act does provide for an exit clause that if the company is not performing well, then it need not continue to incur CSR expenditure.

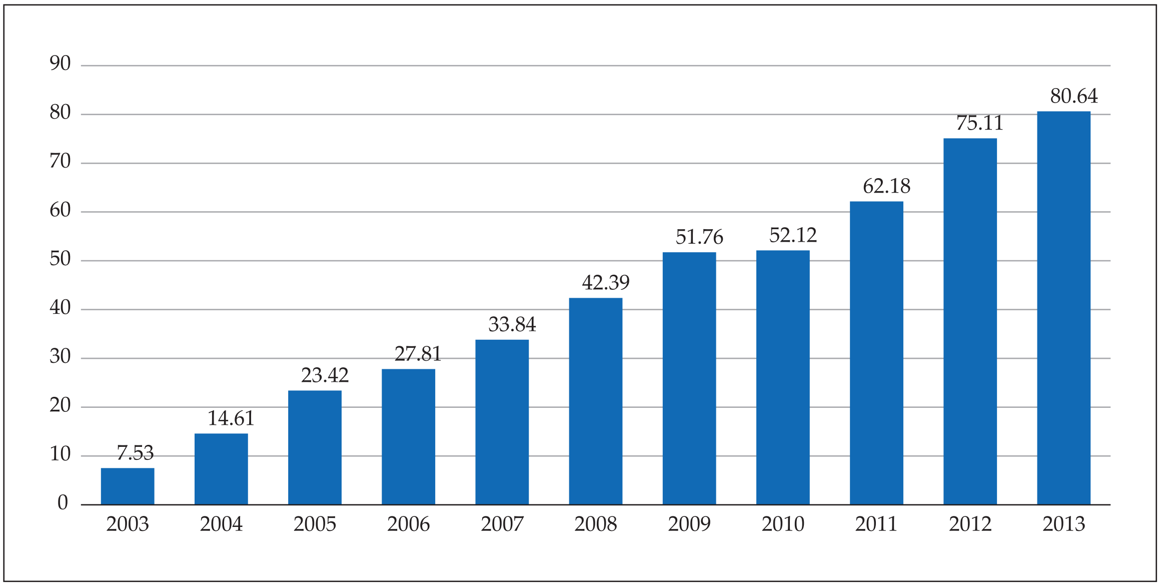
Let me discuss prior to the panel discussion what counts as CSR? Schedule VII of the Act provides the list of activities that corporates can do. If you look at the list below (Box I), we get the sense that the role of business in society that has been envisaged under Section 135 expects corporates to fill up or supplement government efforts in improving the welfare of the needy.

Box I : What counts as CSR ?

- Schedule VII of the Act provides a list of activities that the corporate can potentially undertake, leaving the choice of activities to its discretion.
- Activities relating to:—
  - ✓ (*i*) eradicating extreme hunger and poverty;
  - ✓ (*ii*) promotion of education;
  - ✓ (*iii*) promoting gender equality and empowering women;
  - ✓ (*iv*) reducing child mortality and improving maternal health;
  - ✓ (*v*) combating human immunodeficiency virus (HIV), acquired immune deficiency syndrome (AIDS), malaria and other diseases;
  - ✓ (*vi*) ensuring environmental sustainability;
  - ✓ (*vii*) employment enhancing vocational skills;
  - ✓ (*viii*) social business projects;
  - ✓ (*ix*) contribution to the Prime Minister's National Relief Fund
  - ✓ (*x*) such other matters as may be prescribed.
- Role of Business in Society : Corporates seen as Filling in Welfare Gaps

We have started analysing what the companies were expending on CSR during the voluntary regime. During that time companies were not required to either report or disclose the amount that they were spending. So data on CSR is not readily available. Thus, we took the annual reports of 500 listed Indian firms from 2003 to 2013 and did a content analysis essentially to figure out if CSR was being mentioned in the Director's Report. We observed that on the eve of implementation of mandatory CSR the percentage of top 500 companies reporting CSR has steadily increased and by 2013, 80.6% companies were mentioning CSR somewhere in the director's report (Chart I). So, the idea was really catching up and I think that the companies had figured out something is around the corner for mandatory CSR. I am not presenting the table but our data analysis also showed that 32% of the CSR engagement was in one type of activity and 59% of CSR engagement was in one or two types of activities, so there is little diversification. I am sharing with you these findings because it will help to benchmark what we find under the mandatory CSR regime. According to our classification, CSR activity during the voluntary period is reported to be most prevalent in food, drinking water, sanitation, and health, while education accounted for 17%-18%. If we look at the mandatory CSR spending, you will see that there are similarities or continuity with the voluntary regime in terms of the emphasis on how and where corporates spend.

Chart I : Percentage of Top 500 Companies Reporting CSR : 2003-2013



Finally, we performed a brief analysis of the returns associated with CSR activities, since there is a business aspect to CSR as well. What we found is that during the voluntary regime, in terms of profitability, there were no strong results but in terms of market value, there is some evidence that suggests that CSR improves market value.

Following the analysis of the voluntary regime, we have considered the regime of mandatory CSR. We have done is that we have taken a sample of 1391 NSE-listed firms for the year 2015-16. The reason we did not take 2014-15 was because the data is pretty sparse, since it was just the beginning. We observe that out of the 1391 companies in the sample, 944 qualify for CSR and so they have to spend at least 2% of the average net profits during the three immediately preceding financial years in CSR activities. By this criterion, 914 companies or 68% of the sample qualify and 447 companies do not. Let us look at Table I. Of these 944 companies, if I take the 2% CSR spending criterion, you see that the total CSR mandated expenditure is Rs. 9,139 crore while the actual CSR expenditure is essentially Rs. 8,395 crore, thus indicating a shortfall. But we also observe that some of the companies have spent less and some of them have spent more with overall unspent CSR being Rs. 1,928 crore. The mean CSR mandated expenditure is Rs. 10.57 crore, so it is not that huge a requirement if you look at the average.

Table I : CSR expenditure of NSE listed firms (2015-16)

	CSR Mandated Expenditure (Rs. Crore)	CSR Actual Expenditure (Rs. Crore)	CSR Unspent (Rs. Crore)	CSR Over-compliance (Rs. Crore)
Total	9,139.86	8,395.81	1,928.44	1,184.39
Mean	10.57	9.71	2.23	1.37
Median	1.27	0.99	0	0
Top 10 per cent	15.82	13.85	2.67	0.89
Top 5 per cent	42.76	34.44	8.16	2.5
Top 1 per cent	193.28	196.88	55.56	37.66
Maximum CSR amount to be spent	593.70	651.57	184.69	220

From Table I, we can see that the mean CSR expenditure actually is Rs.9.71 crore and CSR over compliance is about Rs. 1.37 crore. What is interesting is that the top 10% of these companies are on average required to spend Rs. 15.82 crore or more. Then you look at the top 5% and they were on average required to spend Rs. 42 crore or more, but then you go down to top 1%, this is a humongous sum of money. On average companies in this bracket have to spend on CSR, which is Rs. 193 crore. When we looked at the maximum CSR amount that was spent that year, there was a company which was mandated to spend Rs. 593.70 crore and there was a company, we are not going to make judgment right now about whether it is the same company, which had overshot and spent Rs. 651 crore.

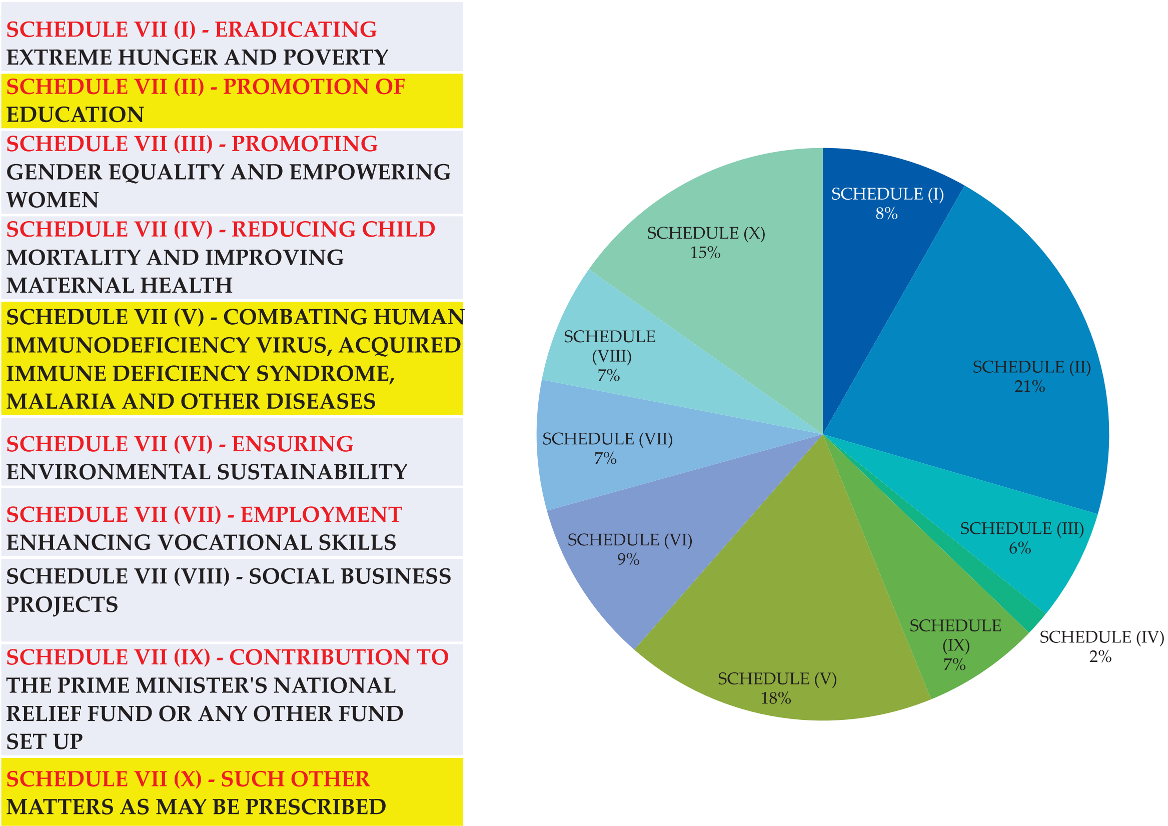
This is the list of top 20 companies (Table II), so the names are out here. Green is basically where you have over compliance among the top 20. Noticeably the levels of over compliance are quite substantial. Reliance, NTPC, ITC and many of these companies essentially in the top 20 have actually spent more than 2% and there are some which have fallen short and the shortfall, as you can see, is as low as 51% among the top 20%.

Table II : Top 20 companies by CSR expenditure (2015-16)

Company Name	CSR Mandated (Rs.)	CSR Expenditure (Rs.)	CSR Expenditure (%)	CSR Unspent (Rs.)	CSR Overspent (Rs.)
Reliance Industries Ltd.	557.78	651.57	116.81	0.00	93.79
N T P C Ltd.	271.35	491.80	181.24	0.00	220.45
Oil & Natural Gas Corpn. Ltd.	593.70	409.01	68.89	184.69	0.00
Tata Consultancy Services Ltd.	360.00	294.23	81.73	65.77	0.00
I T C Ltd.	246.76	247.50	100.30	0.00	0.74
N M D C Ltd.	193.28	210.09	108.70	0.00	16.81
Tata Steel Ltd.	150.00	204.46	136.31	0.00	54.46
Infosys Ltd.	256.01	202.30	79.02	53.71	0.00
Power Finance Corpn. Ltd.	145.79	196.88	135.04	0.00	51.09
I C I C I Bank Ltd.	212.00	171.51	80.90	40.49	0.00
Wipro Ltd.	156.00	159.82	102.45	0.00	3.82
Indian Oil Corpn. Ltd.	141.50	156.68	110.73	0.00	15.18
State Bank of India	0.00	143.92	.	0.00	143.92
Axis Bank Ltd.	163.03	137.41	84.29	25.62	0.00
Rural Electrification Corpn. Ltd.	127.45	128.30	100.67	0.00	0.85
H D F C Bank Ltd.	248.00	127.28	51.32	120.72	0.00
Larsen & Toubro Ltd.	101.46	119.89	118.16	0.00	18.43
Power Grid Corp. of India Ltd.	121.79	115.94	95.20	5.86	0.01
G A I L (India) Ltd.	102.34	104.83	102.43	0.00	2.49
Bharat Petroleum Corp. Ltd.	112.60	95.59	84.89	17.01	0.00
Total for top 20 companies	4260.84	4369.01	-	513.87	622.04
Source: PRAXISCSR Database	All CSR Figures in Rs.	Crore			

Next we look at the distribution of CSR projects by schedule (Chart II). What we have looked at is how companies are spending by schedule. The chart shows the total number of CSR projects that were there in 2015-16 and how were they distributed across the schedules? What we find is that promotion of education was a substantial portion, followed by combating human immunodeficiency virus (HIV), which is basically health you can say. Ms. Subraminian may be able to give us some idea of what the prescribed CSR matters are, but these are essentially the chunks of activities where the mandatory CSR expenditure has gone.

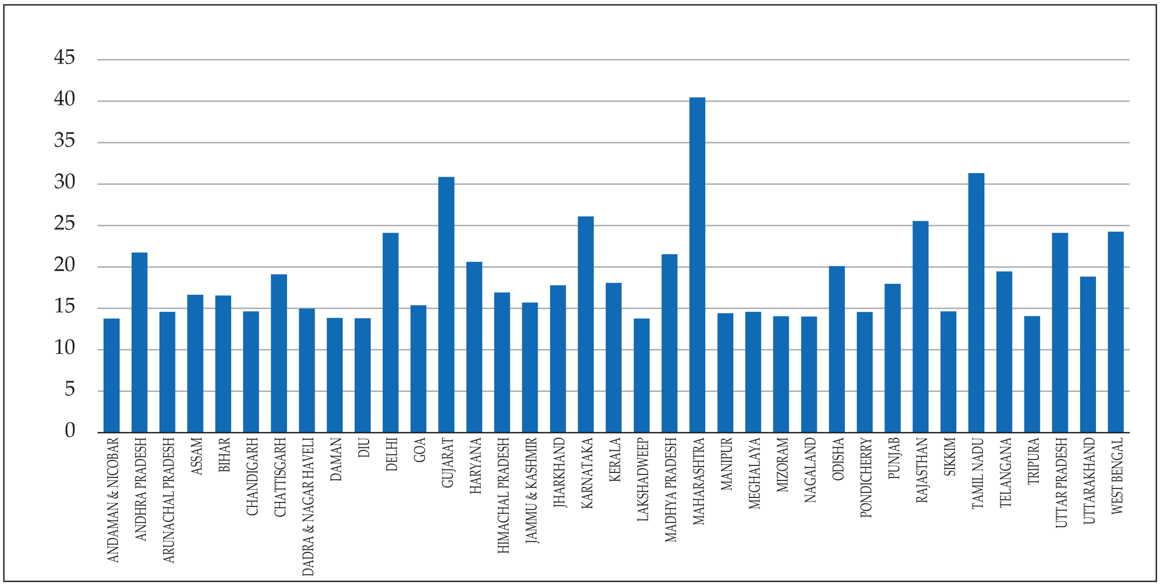
Chart II : % Distribution of CSR Projects by Schedule



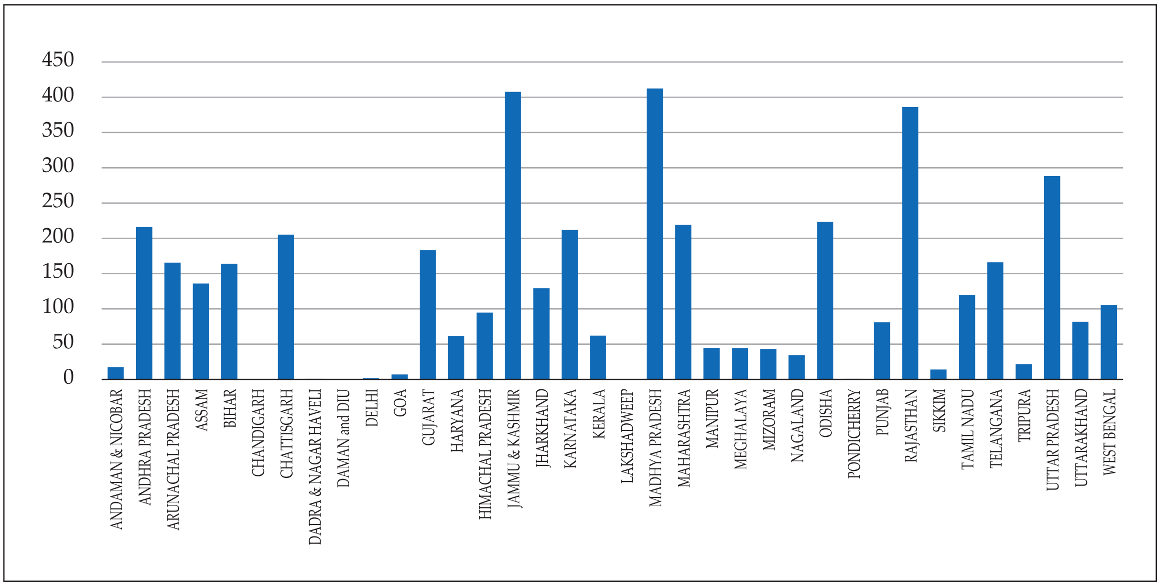
We also realized that there is a possibility of some inequality in terms of geographical distribution of CSR expenditure. The fact that some states are more industrialized than others and as a result, larger companies are concentrated in those states, which in turn benefit from the mandated 2% CSR expenditure as compared to the lesser industrialized states. As expected (Chart III, Panel A), we can see that Maharashtra, Gujarat, and other industrialized states have received substantial number of CSR projects and so there is this distribution where there are some states which seems to benefit more than the others and that could have implications for inequality within the country in terms of the social welfare projects. Next we normalized number of projects by the size of the state (square kilometers covered by number of projects) and the bigger numbers are the states not getting enough CSR funding. If you look at Panel B in Chart III, it more or less remains same as Panel A but it is more stark and you would see that Madhya Pradesh, Jammu and Kashmir, and to some extent Rajasthan where CSR funding is sparse.

Chart III

Panel A: % Distribution of CSR Projects by States



Panel B: Coverage of CSR Projects by States (sq. km/no. of projects)



Finally, given the fact that mandated CSR is there to supplement governmental efforts, we wanted to ask the question that to what extent does mandated CSR bridge the welfare gap. We took all the listed companies and calculated the total mandated CSR expenditure which comes to about Rs. 9,139 crore and compared it with the total social expenditure of the government which is Rs. 8,68,476 crore and you see that mandatory CSR expenditure is just about 1%. If we use this as logic to bridge the welfare gap, it is really a drop in the ocean. So why are companies doing it? There must be some other benefits that we are not being able to capture in this data. To measure the welfare impact of CSR, perhaps, we need to measure aggregate welfare in ways which are not captured in standard measures of welfare.

We can then rationalize or understand why mandated CSR would be effective. We also have to keep in mind that along with the benefits of CSR, there are costs of compliance to mandated CSR, which we need to take into account to understand the net impact of mandatory CSR.

Finally, the road ahead. This is a quote I have taken from someone in the government who essentially said that mandatory CSR provides us with a historical opportunity, process of national regeneration and the Act has the potential to be a game changer for our country. So now we have to essentially evaluate in the context of the discussion so far and the objectives of mandated CSR that whether it has the potential to be a game changer and in what respect? One of the issues I have highlighted for discussion is that some of the companies are going to spend huge sums of money if we go by the 2% criteria. So how do you find adequate projects both in terms of number and in value continuously every year? It is not like companies can take over one set of projects for the next three years but they have to find viable projects every year and sustain these over time. From the governance angle, does it create strain on the company's management or the companies have come up with processes and systems by which mandated CSR activities can be undertaken efficiently without affecting the bottom line of companies.

The second issue is, finding projects which meet a common goal. It is not about saying that we are going to invest in here, one has to find out what is required. Essentially, we have to have NGOs and local government and companies all coming together and agreeing on what could be spent on CSR to make it effective, along with co-ordinating with local agencies for project implementation and project harmonization, while taking into account social and political considerations. Let me conclude with what I think lies in the road ahead. This is an important challenge.

Finally, as the data showed, there is a possibility that CSR is actually going to lead to regional inequality in terms of welfare programs. So, how does one ensure regional equality in CSR spending and social development? These are some of the questions we are going to deliberate in our panel discussion and some more questions which will come up in the course of discussion. Thank you.

Panel discussion: Moving Ahead with Corporate Social Responsibility

Panellists: **Mr. Santhosh Jayaram,** Head, Sustainability and CSR Advisory, KPMG India

Ms. Sanjukta Raiguru, Managing Director and CEO, SBI Foundation

Ms. Shaheen Mistri, CEO, Teach For India

Ms. Gayatri Subramaniam, Indian Institute of Corporate Affairs

Moderator: Dr. Jayati Sarkar, Professor, IGIDR

Somroop Mukherjee: I would like to introduce the Moderator of the session, Professor Jayati Sarkar. She is a Professor of Economics at Indira Gandhi Institute of Development Research and has a PhD from the University of Southern California, USA. Her research interests include corporate ownership and governance in emerging economies, business groups, public sector enterprise reforms and performance. She has published journal articles and book chapters on ownership and corporate governance, and has co-authored a book titled 'Corporate Governance in India'. She is the Editor-in-Chief of the Journal of Interdisciplinary Economics. I leave the floor to Professor Sarkar.

Jayati Sarkar: May I now invite our panelists to take the stage and let me have the pleasure of introducing each one of them.

Mr. Santhosh Jayaram leads one of the biggest sustainability consulting teams in South Asia. At KPMG India, he is Partner and Head, Sustainability and CSR Advisory. He leads his team to work in areas of sustainability strategic advisory, climate change advisory, climate finance and green bonds, sustainability reports and the like. Mr. Jayaram specializes in areas of extra financial risk assessment, responsible business, corporate sustainability, product sustainability, sustainability reporting and climate change advisory. I welcome you and we look forward to listen to your experience on how you are helping corporates to meet this goal.

May I then have the pleasure of introducing Ms. Sanjukta Raiguru. She is the Managing Director and Chief Executive Officer of SBI Foundation, which was founded to bring all the CSR activities of SBI under one umbrella and to continue efforts undertaken by SBI in supporting and uplifting the socio-economically backward sections of the society. Some of the focus areas of the SBI Foundation are healthcare and sanitation, education; both of which we have seen here in our data. Women empowerment, sustainability and environment are other focus areas. Ms. Raiguru brings with her a rich experience of banking operations and academics, so here we are going to basically get the perspective of how corporates are figuring out to spend that 2% every year and how is she managing. Welcome Sanjukta.

Now, may I have the pleasure of introducing Ms. Shaheen Mistri. She is the CEO of Teach for India and serves as one of its founding board members. She founded the first Akanksha Centre in 1989 enrolling 15 children and eventually launched Teach for India in 2008. TFI as it is more commonly known, has been since inception working tirelessly to ensure that one day all children will attain an excellent education, so this is what TFI motto is and I am quoting it. Among her many accomplishments, Shaheen has been an Ashoka Fellow, a Global Leader for Tomorrow at the World Economic Forum and an Asia Society 21 leader. Welcome Shaheen and we would really like to hear from you how NGOs like TFI have benefited or what have been the changes that have happened after companies have shifted to this mandatory CSR regime. Has it been better or is it the same story?

Last but not the least, I invite Ms. Gayatri Subramaniam on stage. She has academic and industrial experience of more than 30 years. Ms. Subramaniam has been associated with Indian Institute of Corporate Affairs (IICA) since its inception. Her main area of work is to contribute towards policy advisory service and undertake capacity building and knowledge dissemination initiatives in CSR. She has been involved in formulating the new legislation of CSR in India and we really would want to know what is the story behind the scenes. She is the convener for National Foundation for Corporate Social Responsibility (NFCSR), a unique platform created for government, corporate, and NGOs for taking up development and sustainable initiatives at a national level. At present, she is heading the implementation agencies hub of IICA. We welcome you Gayatri and we would really like to know how this all came about and what are the challenges that you are facing in terms of implementation.

With this short introduction, we will start the panel discussion. Each panelist would make his or her opening statement for about seven to eight minutes and then we would discuss some of the issues that have been raised through my presentation as well as what would come out of their opening statements. After that we are going to take questions from the audience and then I am going to conclude. Santhosh, would you like to flag off the discussion.

Santhosh Jayaram: First of all, thanks to NSE for calling me here and thanks to Professor Jayati Sarkar for the introductory remarks. I have been involved with CSR right from the day when the Companies Act and Section 135 were in the draft stages. When the Act was put as a draft, we had consultations with various industry players. The initial reaction was that it is a tax and in response we used to give a dataset, which showed that if you look at the government spending in these areas, what we are accounting here from the whole of corporate India will not even qualify for 1%. And so we are not looking at it as a kind of a big change which the corporates can do, but an explicit call to corporate India to be partners in the development space.

Amendments of the Companies Act were more about improving the governance standards in India. The trust in corporate India was at its lowest with rampant scams being the order of the day. A need was therefore felt to revise certain things so as to bring about an improvement in the then prevalent level of corporate governance in the country. Now, where does CSR fit in here? If you remember the decade before the law was implemented, in eastern parts of India, you would find that while the government might have given approval for a particular project, it was the society which was against it. Those cases were considered and the Act also very clearly mentions that CSR shall be undertaken preferably in the local area. So, the intention was to improve the trust quotient and also the second part of it is, "better the governance around CSR", which is the critical part of CSR.

Now, when I say better governance around CSR, let me give you an example from a pre-Companies Act era of how CSR used to be. I am not kind of generalizing it but when I take an example, and having said that, when I take an example, the usual disclaimer goes: Any resemblances to any person or a company is purely coincidental and nobody living or dead is referred in this. Let us say that I am the chairman of a company which is listed. I run an educational institution as a person but not as part of the company. Every year, I write a cheque from the listed company of about 3 crores to that particular educational institution and call it as CSR. But now, the board-level committee with an independent director has to approve this and also the company has to disclose the same. If you look at the disclosure template which has been created, it talks about what is the project about, in which state or which place the project is happening, how much were the spending, who are the partners etc. This is the level of disclosure that is required now. So, what the Act is primarily trying to do is to improve the image of corporates in the local community. The second part of it is the governance per se around the CSR. These are the two things which the Act is trying to do.

Now, I am skipping many of the statistics because it has been already covered. We do an annual survey of CSR activities of the top 100 listed companies, analyze responses and put it out in public domain. We find that there has been an improvement in terms of the expenditures and many more parameters compared to the previous years. The average spent per company has increased 15%. There are 52 companies out of the top 100, which spent 2% or more. There are 7 companies who are not required to spend as they have been making losses for the last three years, but, they still spent. Sixty three percent of the overall spending of the top 100 goes into only these two areas: a) Health and Sanitation, b) Education and Skills. People initially thought PM Relief Fund will provide good tax benefits and all companies will put the money over there. But it ranks 9th among various kinds of CSR expenditure.

Of course, states like Maharashtra and Gujarat get the most of CSR funding. The important point is that this year what we have found, and it is very important, that although the overall expenditure has been increasing, the total number of projects in the top 100 reduced by 33%. Now, this is significant and we consider it to be a good thing because rather than spreading out, companies are focusing on more concentrated efforts.

When you look into governance per se, 90%of the companies have standalone CSR committee. Earlier it used to be a combined committee. As per the law, the CSR committee shall consist of minimum three directors, out of which at least one director shall be an independent director. Out of the top 100, 64% companies have more than 3 directors, 47% have more than 1 independent directors and 55% have women committee members. The highest number of members observed in the top 100 is 8.

The report also compares the PSUs and non-PSUs. As a closing remark, what I would say is that there is a clear intention behind the Act and analysis of last 2 years shows notable improvements. We hope this continues and marks a new era in the development sector. Thank you.

Sanjukta Raiguru: Let me begin by sharing with you the experience of SBI Foundation's CSR journey in the last one year and nine months. Post the CSR Act 2014, the board thought that now we should have a vehicle to seriously pursue CSR for the entire SBI group--all the banks, the associates, and all the non-banking subsidiaries. That was how the SBI Foundation was born and I had the privilege of setting up the foundation. Today, after one year and nine months, I am proud to tell you that we are on the right track. Basically, how did the change come about? The change was that previously the entire group was undertaking CSR activities in an unorganized manner to achieve the necessary target. However, when the SBI Foundation was established, we had to switch from a 'philanthropy' mode to a 'project' mode, which turned out to be a fairly daunting task, owing to the lack of expertise. After all, our whole team was essentially a group of bankers with practically nil experience in the domain of CSR. As a result, a large part of our time was devoted to gain knowledge about the field. The constant interactions with the whole spectrum of stakeholders in the ecosystem eventually proved to be a great learning experience. What we discovered was that owing to us being new to the CSR ecosystem, there was, to some degree, a healthy suspicion surrounding us. We initially faced roadblocks in the form of compliance related issues with regard to the CSR Act. The SBI group being omnipresent in India, deciding upon the nature and the scale of the projects itself turned out to be a mammoth task. We eventually identified our four broad focus areas--Health and Sanitation, Education and Skill Building, Women Empowerment and Rural Development. Broadly, we found that we must reach out to the states which are starved of CSR funds, and there are sectors which are also starved of funds. So, there are certain sectors where funds go, like health and sanitation are at the top of it, followed by education and then the rest. Also, our board has a special corner for women. The data showed that the projects are very sparse in rest of the sectors.

Secondly, we learnt that NGOs promise a lot without having the capability. We found a good number of small NGOs in interior pockets of different states, which are doing excellent work but are not able to come to the mainstream because they are not the real big ones in the market. I thought that we need to have a very inclusive policy by which we can also bring them in. Our due diligence has to be such that we have to include the small NGOs who do excellent work on the ground in the hinterland. We get hundreds of mails, but no mails come from any NGOs from the North-East or from Jammu and Kashmir. All the mails come primarily from the metropolitan cities.

The third issue is monitoring. The introduction of the CSR rule led to a lot of upheaval in the entire ecosystem. The shift from funding and forget to funding a project with a stated objective to be achieved within a timeline with measurable impact has generated a lot of upheaval among all the stakeholders--the founder as well as the NGOs or implementing agencies, as each one struggled to discover the best ways to satisfy all; the Corporates, NGOs, Auditors (Compliance) etc.

Developing a monitoring system for each and every kind of project, starting with fund disbursement, utilisation, progress on ground and the impact it is making, has been another challenge.

These are the challenges that we have faced but, at the end of it, we are today able to partner with the smallest of the NGOs and also the biggest of the NGOs. We are working in the field of child health, child education (especially girl child education), maternal health of women and malnutrition. These are our focus areas. Thank you so much.

Jayati Sarkar: Thank you. I am sure you are going to share with us how you have met the challenges, and what are the changes in policies that you have made in order to include the smaller NGOs.

Shaheen Mistri: Hi everybody, good evening. I would like to begin by expressing tremendous gratitude for the Act and while of course there is always, like with everything, scope for improvement and how it gets implemented. For an organization like ours with a very big dream that one day all children in the country will attain excellent education, to be able to leverage that kind of funding and that kind of giving has been exceptional. I do not think we would be able to do the work that we do without it, so a lot of gratitude to everyone in this room and beyond who has given, who has thought about giving and who is associated with the Act. But I thought I would use my opening remarks today, I am a little bit of a dreamer, so bear with me. I thought, I use my time to share my dream for the mandatory CSR Act.

My dream is that we think about the scope of the Act in a very different way, in a much bigger way, and so if you visualize this, what I see in my dream is, people like yourselves at lunch time in your companies sitting around in the cafeteria, talking about the incredible opportunity to make a difference to the world that your company is allowing you. I mean think about it, without putting your hand in your own pocket to give money, you have the opportunity to change something and in some of the larger companies that is really, really significant. And I see a world where you are competing to get on to those CSR committees because you really understand the value of what that stands for. I will narrate two quick stories. All my life is around children, so they are about kids.

Couple of weeks ago, I got a mail from a mother of a six-year-old child who said that my son wants to meet you. His name was Malhar and he wanted to meet me because what he had done was that he had baked his own chocolates, had sold them and then he had done research online about where he wanted to give the money. He had come to present several thousand rupees to me from the sales of his chocolates, and I thought that it is a small act but a six year old able to do that is incredible and the excitement and the joy that he got from that.

Then a very different and much bigger story, which is very close to my heart. Few years ago, when I was still at Akanksha, one of my kids Lateef, very tragically, very suddenly, got a respiratory illness and passed away. But the incredible part of the story is the night before he passed away, his grandfather who was his favorite person in the world gave him Rs. 14,000 and asked him to go to a private hospital because he was very sick. Lateef's grandfather, who had worked for many months as a watchman and saved that Rs. 14,000, had just stopped working. As Lateef did not want his grandfather to go back to work, he quietly took the Rs. 14,000, hid it back in the house and went to a government hospital and he passed away 12 hours after that. That was to me a real turning point in my life because I thought I understood what it meant to give and I realized through Lateef's story that I had no idea about our capacity, to be able to give, not as companies but as human beings to be able to give.

Three really quick thoughts in my learning and my journey on giving. The first is, let us always make sure that we are giving in a way that we are able to cater to people's needs. The second one is, can we dream about CSR not just being about money? I work in an organization where today 1200 young people, some of the brightest minds in the country leave their jobs at multinational companies and teach full time for two years in a government school. In the process, they become part of a community of 3000 people today who will look after them. Yes, they have made financial sacrifices--they get paid Rs. 17,000 every month at Teach for India, a very paltry sum in comparison to what they were getting in their previous jobs. But look at the social capital they earn. Every time I walk into a classroom, I am flooded with kids showering me with love. In what office does that ever happen? So can we think about CSR as something beyond money?

The last quick point is about realizing and I think all of us in this room know that when we give, we get so much back and I think if we really believe and internalize this, we will not need to use the word 'mandatory'. Instead, we will come to work saying, what an incredible opportunity the country has given us to make India better and in the process of making India better, make ourselves a little bit better as human beings as well.

Jayati Sarkar: Thank you, Shaheen We will take this forward. Gayatri, please.

Gayatri Subramaniam: A very good evening, everyone. At the outset, I would like to thank NSE for inviting me. I think being the last speaker has its own advantages and disadvantages. In this panel, we have a dreamer who is thinking about how to give and how to make maximum out of it. We have an academician who is pointing out what difference this 1% out of government's approximately 9 lakh crores will make. Being a part of the entire evolution as Santhosh put it, I am feeling very proud. In fact, I would say it is not even mixed feelings. I used to have mixed feelings because the evolvement was not so easy. On the contrary, it was quite a rollercoaster ride. I am reminded of that cold December morning in 2009 when Smt. Pratibha Devisingh Patilji, the President of India back then, released this eight page intent document and predicted that the document had the potential to create a revolution; and it has. After that, in 2010 when it was mandated for public sector undertakings, I was in the same room wherein all the representatives from Maharatnas, Navratnas and various corporate honchos were sitting. The reaction was what next, how are we going to do it, another law?

In 2011, when National Voluntary Guidelines were released and were mandated by SEBI, again the same questions--how, why and what? Similarly, it was mandated for companies in 2013. So, now we are talking about Companies Act. Companies Act has 470 sections. But the most talked about, the most chaotic one which is still being talked about in such forums, I think I have been talking about it every day, Santhosh has been a part of it, is the Section 135 only. And as you rightly put it, Professor Sarkar, it is like 1% against government's 100% and how many companies? There are around 12 lakh registered companies with the Ministry of Corporate Affairs. How many companies fall in the ambit of mandatory CSR? Not even 1% of the total number of companies in India i.e. only around ten thousand companies in India. What are they supposed to do? To put a CSR committee in place and make a policy. The board makes sure that the activities mentioned in the policy are being undertaken and if not done, disclose reasons. They are not even supposed to spend 2%, they just need to disclose reasons. So where do we stand today after two years of the Act? We stand at a landscape wherein there are these 10,000 companies wondering what to do, how to do, where to spend; and there are 3.3 million NGOs supposedly who are willing to help but then as my friend from SBI Foundation said, there is huge trust deficit between companies and NGOs.

The Act was passed in August 2013. From 1st April, 2014 companies were supposed to spend. September 2015 was the time when corporates were supposed to inform CSR spending to the ministry and file their returns. They were given three months' extension, so December 31st was the last date when they were supposed to give their figures. When we got the figures and analyzed them in early 2016, out of around 10,000 companies, 7,334 reported only the expenditure and out of that, only 3,139 companies spent, but the best part is that out of Rs. 11,883 crore, almost Rs. 8,803 crore were actually spent. That means 74%. And we have been wondering whether it was done or not, but I would like to share that it was spent. It is a different story that lowerhanging fruits were caught before because most of it was spent on education, health and the ideas which were like on art, culture, heritage, Olympic games, alms for veterans etc. were not much considered by these companies.

We also did an analysis of how this money was spent because I think over the last two years we have been talking about NGO and corporate partnerships. But again, the good news is that around 39% of the money was spent through NGOs and around 53% was spent directly. I would say that what we are seeing is just the 10% of the iceberg, 90% is still below water; it has just been two years, and so we should be very optimistic. It has already created change. It is a game changer and in fact, it has happened only in India because it is the only country where CSR has been mandated. I think each one of you can, as Shaheen put it, contribute towards it and I think we can all make it really, really successful.

Jayati Sarkar: Thank you Gayatri**.** Thank you for all your valuable opening comments. Without further ado, let us begin the panel discussion. I just wanted to take up a few of these issues. As Sanjukta was saying that there is a particular way in which you have to look into how to spend the 2% or 1% on CSR. My question is, has mandated CSR led to changes in the way companies are strategizing, organizing, implementing CSR from the voluntary regime to the mandated regime? I think each of you can give your insights on that. We shall start with you, Mr. Jayaram.

Santhosh Jayaram: Definitely yes. As Sanjukta had said that it was a kind of a change, which companies have to make it project-based. As I discussed, even when spending is increasing, we have seen a reduction in number of projects, which is a welcome sign that there is focus on projects which are underway. These are clear indications that the governance structures are being put in place. The monitoring and evaluation is also getting stronger, as the board committee is now accountable. So, what I would say is, the way in which CSR is getting implemented is changing, but we also have to remember the point which you made. I want to reiterate that there are three players in this: The government, which has a role to play, then there is the corporate and there is the civil society or specifically the NGO as implementation partner. It is a collaborative effort.

Now, the challenge is that if the corporates are still continuing to do what the government was doing, it is not going to be successful. How the private sector can play the role of a catalyst in this, is something which many of the companies are looking into, as they want to stand out. New models are being tried out, which the government using public money will not be able to do and maybe out of these, there will be some good models which would evolve.

Another development is that there is a whole new player evolving in this CSR regime called the aggregator, whose role is to come in between the NGOs and the corporates. Impact funding and social impact bonds are some of the new things, which we are already hearing noises about and it is going to be a kind of radical shift in the way social sector is evolving because of the CSR revolution.

Sanjukta Raiguru: I could not agree more on the way the Act has brought about a change in the landscape, particularly in the way how the corporate sector has started doing CSR in a meaningful and impactful way which is the project mode. However, with the project mode comes the problem of really getting the project and the capability. But nevertheless, within the limitations, there is scope to experiment a particular model, a particular unique way of approaching a problem statement. I think corporates can continue with experimenting or giving scope to realize or fructify or mature their model, and that would probably add value. That is one good thing that I am finding.

Take girl child education for example. The traditional model would be to open a school and impart education. But one unique model/approach can be based on the problem statement that the girl child in villages is another domestic hand and many times proxies the mother as a caretaker at home and therefore she is not sent to school. So, there is an NGO that imparts education at a community centre by gathering girls of the village during hours when they are spared of work at home. The NGO imparts education not in the structured way but by giving them relevant life skills along with reading and writing. This may not be possible with public money. Corporates have promoted such unique models and later on Governments have emulated.

So, corporates can really promote the NGOs, which approach the problem in their own unique way, which the government does not. There are models in a public-private partnership where NGOs are working with the government, and we have found there are several models that NGOs have adopted from the state government. There is scope, nevertheless. Compliance is a big thing. The KYC of the NGOs, the regulatory, etc. Also, the regulatory part of it and the corporate governance part of it has to be in place, otherwise, it would be difficult to do. And finally, the monitoring. This has to be every quarter, otherwise if you always go on measuring, then when do they work?

Jayati Sarkar: I want to ask the next question to Shaheen. The mandatory regime has increased work related to compliance, reporting and reducing the trust deficit. Is a lot of time going into that?

Shaheen Mistri: Yes, I think it varies so much from company to company. I think monitoring is a challenge and sometimes it does get very tedious if you do not have a large team. Another challenge, sometimes, is a little bit of confusion/rigidity about which parts of your CSR budget can actually get funded. So, easier to implement and monitor, and visible projects get funded very easily. But then you are stuck with not knowing how to raise the rest of the budget whereas before the mandatory CSR Act, companies were quite willing to absorb a little bit of that part of the budget along with the programmed projects. So, these are two of the many challenges.

Gayatri Subramaniam: I would like to say that we must not forget that most players in the corporate sector may be first timers. Also, those who have been doing good work before just had to tweak their systems. It is the set of big corporations, especially family-owned businesses, who were asked to voluntarily do CSR for the first time and so their first reaction is "How do we evade this?" Now that it has become a part of compliance, the reaction has changed to how do we go about it. As I mentioned earlier, there exists a huge trust deficit, so the intention of the ministry as well as that of the Indian Institute of Corporate Affairs was to bring in those two actors together so that we can achieve a multiplier effect in a more comprehensive manner by leveraging the project management skills of NGOs and the financial and other governance aspects of corporates. So, it has to be done in a partnership, otherwise just giving it to NGO and relaxing or the corporate doing it on its own is not going to work.

Jayati Sarkar: My presentation, as well as Mr. Jayaram's report and as Sanjukta was saying, corporates are currently funding low-hanging fruits, as it is very easy to spend on these projects and these are projects which can be supported and scaled up. However, in schedule VII there are many important areas where the government wants corporates to participate but that is not happening. Same with respect to unequal CSR funding among the states. So, how do you think the government can do something about this? Or, is there any mechanism that the corporate would want to put in because, from the point of view of the corporates, they would want to go to easier states or wherever implementation is easier and then get the mandate done. So, is there any suggestion each of you would want to make, as to how we can solve this potential problem that is actually showing up in the data?

Santhosh Jayaram: I will make it very brief, no more prescriptions to the corporates. I think it will take a natural evolution and the early signs in this evolution are encouraging. Prescriptions will make it very difficult to operationalize.

Shaheen Mistri: Can I just add one thought? I am just thinking so much about purpose. Do we talk enough in companies about the purpose of why we are doing this? If the purpose is genuinely to make something better, then it does not become about compliance. If the purpose is just how do I do this so that I can report it, it is a very different motivation and I wonder if there can be any more dialogue around that. If you see the value and the intrinsic value of the Act, all of this will shift the way in which we operate.

Sanjukta Raiguru: Taking the point of Shaheen, purpose is important, the intent is important. But at the same time, how do you prove the purpose on paper when you take an executive decision? You like a project, believe that it can make a great impact on the field, but it is more of a process-oriented project which has less of tangibles, which you cannot show. So, it becomes extremely difficult to justify on paper. And at the end of it, you are subject to a lot of questioning that why did you do this and why did you not select somebody else. Each NGO is different, each one has a unique thing. Definitely, you build in the project proposal that Justifies why you are taking the decision, that these are the strengths of the project and you expect that it will make an impact in future. The results will only show after five years, but there is no patience in the system to wait for that. How does the Act take care of it? That is the difficulty with the corporates. Though we have a lot of empathy, our hands are also tied. We understand the intent, there are good number of NGOs who come to us and we find a lot of value in that but it becomes very difficult to justify our executive decision.

Gayatri Subramaniam: Actually my experience is that peer pressure also plays a very important role. A corporate in the banking sector would like to do what other banks are doing. It is the same with the manufacturing units as well. So, it is very important for bodies and chambers to take their role seriously of integrating those efforts. All said and done, it is just two years and the beginning has been made. What corporates want is doable, scalable, and replicable projects. Because their profits are going to go up and we have anticipated an increase of 8-10% in CSR spending every year, the projects have to be sustainable. In that case, they will put in a lot of thinking before parting with their hard earned money. That is why I said, the industrial chambers and bodies like National Stock Exchange need to play their role as a facilitator and enabler very seriously.

Jayati Sarkar: Before I open the floor for questions, there is one question that I have; it is about the road ahead. If each of you can list one thing that you would want to see to make this policy more successful based on the experience that you have had in the last two years. We can start with Gayatri.

Gayatri Subramaniam: Balance and empathy in all the actors who need to do CSR.

Shaheen Mistri: I would repeat the same point, moving from compliance to purpose, by really asking ourselves why does a certain issue matter.

Sanjukta Raiguru: Compliance is certainly an integral part but the purpose is also important. Therefore a balance has to be struck between purpose and compliance. Compliance is an absolute essential but too much emphasis on compliance is not a good thing either.

Santhosh Jayaram: For me, it would be innovation. The opportunity is that some of the CSR could be used to enhance the innovation capability around development challenges and that can be used to unlock government funds.

Jayati Sarkar: Thank you, so let us take some questions.

Participant: A high level CSR committee pointed out that it is all about 'comply or explain', and they said that you make it the spirit of the Act. Why Section 135 was implemented in the first place, should be looked into. MCA comes out with the circular saying that schedule VII should be interpreted liberally and you should account for a lot of things within what is mentioned in schedule VII. Now, despite all this, we see that mandating CSR through section 135 has actually become more like an expenditure than being implemented in spirit because what we hear in board meetings is that the company will we be penalized for not meeting mandated CSR expenditure, etc. As Shaheen pointed out, we do not hear about the purpose. So are we expecting corporates to move towards finding purpose in the near future or how do we look at it?

Santhosh Jayaram: Let me give you one example. I have seen a number of CSR committees going to the field and now seeing some of those kind of projects. You are not expecting the 10,000 odd companies committed to do that from the first year itself. A transformation is happening and as Sanjukta also said, the corporate has an obligation to comply, which cannot be forgotten. As a listed company, they are supposed to tell the shareholders how they are spending on CSR activities, for what purpose, etc. There are obligations so we should not miss them. But what I am trying to say here is that the committee is doing it with a lot of heart, where the people are going to the field, seeing the beneficiaries there and interacting with the beneficiaries. All these things are happening.

Gayatri Subramaniam: I will just like to add a point. Many of the companies are also seeing it as an opportunity to lever up on their brand equity. Maybe they are doing it out of compliance or compulsion but they are also considering what good CSR can do to their company. That is one aspect which we have seen in many companies. The thinking is, we have come to a stage where we need to do it, so let us do it right.

Shaheen Mistri: I will just add one quick point. I request to go and change the conversation. I think that is where change starts with all of us. In those conversations, if we can introduce those ideas, suggest the field visits, talk about the purpose. Of course, ultimately it is about benefitting the company and the others, but shifting the conversation is in our hands.

Participant: This question is for Ms. Subramaniam. We face a very practical challenge--rule says that whatever you are doing in normal course of business will not be considered a CSR activity. For us who belong to the aviation sector, we get a lot of requests from the underprivileged section where they need to travel from far off places or a cargo needs to be sent. However, because of the rule, we are not able to give them free air tickets which becomes a big hindrance. As a travel company, we happen to get lot of requests like this. So, how do we go about it?

Gayatri Subramaniam: In case it is part of a project, it can be included in the project cost. But if you have just started flying them free of cost, that is not going to be considered as CSR activity. You need to have this travel as the part of a project, which should have the inputs, the timelines, the expected outputs and the outcome very clearly written in your project report.

Participant: Can we have a project where we fund travel for all medical patients? Like this is a project that is only about funding the travel for medical purposes?

Gayatri Subramaniam: As of now, there is no auditing by the ministry or nobody is asking you whether what you have done is CSR or not. So, as long as your auditors are satisfied, it is fine. But essentially, if you can show a certain activity as part of your project, it can be considered as CSR expenditure.

Participant: I have two questions. Firstly, don't you think CSR in kind should be allowed? While the law does not permit it, can it be allowed in the near future? I also wanted to seek your views on how the administrative overheads or capacity building expenses are defined and whether the salaries paid to the CSR team, etc. is a part of the overall CSR expenditure?

Gayatri Subramaniam: CSR in kind is not accepted and it has been clarified in the 'Frequently Asked Questions'. In case you want to send in a request, you may send it to the ministry's CSR cell. As far as rules are concerned, they are quite dynamic in nature. In case there comes a strong and viable suggestion, the rules can be altered without much bureaucratic formalities.

Regarding the second part of your question, admin overheads and other expenses is up to 5% of the mandatory CSR expenditure (2%). The high-level committee which we spoke about has recommended it to be 10% but that is still under consideration. In fact salaries of CSR staff, as it has been clarified in Frequently Asked Questions, should be part of managing the project cost. CSR team's salary is a debatable issue. As I said, if the auditor is satisfied, the ministry is not going to hound you with questions.

Nirmal Mohanty: I have a couple of questions. The first one is, you mentioned that in case the companies fall short on compliance, they can still explain. The first year is over, what are the kind of explanations that are coming up with regard to most companies?

Gayatri Subramaniam: That is a very good question. The reasons that have been offered by some companies are quite strange and at times not relevant. The most common reason offered is lack of awareness that the company falls in the ambit of mandatory CSR. Another reason was paucity of good projects or lack of good implementing agencies.

Nirmal Mohanty: The second question is whether it is possible for companies to tie up with local bodies, municipalities and so on to do CSR activities? Have there been instances of those?

Gayatri Subramaniam: Yes, there have been instances and I believe it should be done. The Act clearly says that contribution to any political party is not allowed, but at the same time when a project is undertaken, it is important that the local bodies are taken into consideration because stakeholder consultation is a must. When companies need an assessment of any project, it is very important that local stakeholders and the beneficiaries come first in mind. For example, when the company is doing mobilization of beneficiaries or finding out what is needed in the area, it is important to work with local bodies and local governments because the government schemes can be supplemented or complemented through CSR interventions. Companies can work with local bodies, BDOs and panchayats because ultimately whatever intervention it undertakes has to be handed over to the community. So if it is done through panchayat or through BDOs, it will always be helpful because that will help in operations and maintenance in the long run.

Participant: If the CSR expenditure is allocated by the company and the budget is handed over to an NGO, and then the NGO vanishes, will it still qualify as a CSR expenditure because the company has already spent the money?

Gayatri Subramaniam: Again at the cost of repeating, I would say in case if your internal and external auditors are able to justify it, it is fine as of now. This is because, at present there are no auditing standards or any accounting standards which have been implemented by Ministry of Corporate Affairs. When the Minister of Corporate Affairs had presented this Act he called it a leap of faith. Even then, the rules specified that the selected NGO must have been in existence for at least three years, have audited accounts, a permanent address and a history of doing CSR projects. Therefore, it is important that a thorough due diligence be conducted before choosing the NGO.

Participant: My question is to Mr. Jayaram and also to the rest of the panel. So you talked about the intent of the law, the law taking shape in terms of leveraging private sector expertise, innovation or maybe collaboration. In this regard, what is the future pathway for CSR? That is, is it going to be a natural evolution or is it going to be policy driven?

Santhosh Jayaram: I think the policy part of it is in place already. So from here onwards, I am not a person who would desire more and more prescriptions be saddled upon this. We have witnessed dramatic improvements in the past two years, and that too not merely in terms of numbers. We have seen a dramatic change in the kind of involvement the organizations are currently having with their CSR projects. I am also very hopeful when I said innovation is the critical part and evolution will make us explore many new areas.

Participant: Have notices been given to companies who have not spent? Can you elaborate on the 'comply or explain' provision in the Act?

Gayatri Subramaniam: It is very important to know that the Act says that companies have to constitute a CSR committee, which will frame CSR policy and the board will approve the policy and ensure that the CSR activities are undertaken. Companies have to spend 2% or disclose reasons for not spending. All of this is mandatory. The committee has to be given responsibility, the policy has to go on public domain and 2% has to be set out. Only the last part, if not spent, the company has to explain reasons. Notices has gone to those companies who have not followed these.

Participant: My question is not really a question, but a suggestion going forward. I come from Tata Institute of Social Sciences (TISS) and with two years of experience. We are the national CSR hub. What I believe is really necessary and the corporates should take seriously is, to build the capacities of people in the corporate sector, make them understand what CSR is and make them feel what the NGO sector is like. From my experience, I know that it is not like corporate to deal with the NGOs, but the NGO sector has got their own strengths and therefore, we should try to develop a better understanding about the NGO sector and only then can the companies bring about a change. Otherwise, there will always be conflicts. Mere compliance is not going to bring about any change in the sector. I have worked with Tata Trust for 40 years and my understanding of things is that if companies really want to bring about a change in the community, they have to work with the community in the field, try to understand their problems and try to build confidence rather than having a top-bottom approach where companies provide the money and give directions. However, only building capacity as a corporate will not entail much benefit unless the capacity of the NGOs is also built. Only providing money to the NGOs will not have much effect; seminars and workshops must also be held for the NGOs to ensure capacity building, so as to make CSR more effective.

Second thing is that it is important that the corporates encourage voluntary CSR activities undertaken by the employees because if they do not inculcate the spirit of voluntarism and say "I am giving you money and be done with it", I think, the corporates will not achieve the purpose for which the money was given.

Jayati Sarkar: Thank you very much and that is a really wonderful note to end this panel discussion. We need more co-operation from the major players in this mandated CSR scenario and as we can see from the discussion that in two years we have come a substantial way in which corporates, NGOs and the government have tried to make the CSR policy successful. There are some implementation challenges which are going to be taken care of as a note of optimism is prevalent everywhere. I would like to conclude by reminding you the number I had shown and I had said that 1.05% is the mandated CSR expenditure as a percentage of entire social expenditure. We have to figure out ways to measure its impact beyond that 1.05% and maybe if we bring in the purpose and we bring in other metrics of evaluation, then possibly we would understand that mandated CSR may turn out to be a game changer. Thank you very much for all your attention. I thank all our panelists for the productive discussion on mandated CSR. We have learnt a lot from their expertise and points of view.

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