

CORPORATE SOCIAL REponsibility OF BUSINESS AS A BASE OF FRAUD DETERRENCE

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ABSTRACT

The core objective of the business entities, in the current world, underwent a drastic transformation from the narrow perspective of profit maximization to a broader and dimensional principle of Value Maximisation. Every organization thrive to achieve this objective on all counts, notwithstanding the penetrating risk factors. It has been felt by the experts that every business entity, need to uphold the Social Responsibility Principle while attempting to reach the sustainable goals. Though the Social Responsibility of the corporate convey at the outset, the quintessence of charity, the experts share their piece of heart with respect to the principle in a manner whereby, it need to be contemplated as a market opportunity. These thoughts again critically focus towards attaining the top and the bottom lines of the business, vindicating the esteem objectives. While making every effort to set foot on the nucleus, the business will have to encounter with various risk factors, which acme the Fraud Risk factors, being the most damaging constituent of the financials of the business. Hence the people who are charged with the responsibility of governance of the business will have to conceptualize these factors and delineate the Internal controls to narrow down the risky elements to a level acceptable and controllable to the business. The business management in this regard need to consider all ethical, social and legal factors and bring together all these aspects to eliminate the fraud risks and to bring to the hand fold the concept of value.

INTRODUCTION

The business throughout the world, now a days undergo vast changes in terms of its modus operandi. The business conventionally in the past were upholding the narrow concept of maximization of the bottom line. But in the current global business environment, there has been a paradigm shift in its core objective from the above profit maximization concept to a broader aspect of Value maximization, which paves a way for any business to attain the sustainability in terms of its thriving operations. The corporate social responsibility of the business play a significant role in enhancing the value of any enterprise. The ultimate responsibility of any business will be towards maintaining an exceptionally conducive environment and the most delighted people who are directly or indirectly related to the business, to ensure that the Profits along with the cash flows always follow the business and not vice versa. The effects of the business in the society at large and the environment are keenly observed today by the stakeholders. As the globalization emerge as the need of the hour for most of the corporates, the need to implement rich and progressive business practices and controls with a funneled focus towards positive environmental and stakeholder policies is inevitable. The organizations which uphold these corporate social responsibility principles sustainably would be able to transform their investments into productive benefits in the long run.

SOCIAL RESPONSIBILITY

Social Responsibility is defined as, “The obligation of an organization’s management towards the welfare and interest of the society which provides the environment and resources to survive and flourish, and which is affected by the organization’s actions and policies.” The focus of any Socially Responsible organization would be towards protecting the society, the environment and its resources, rather than solely aiming to make profits. These business corporates need not have to run after the profits but will create a scenario whereby the profit follows the business on account of autoschediastic, socially committed operations. The CSR definition used by Business for Social Responsibility is: "Operating a business in a manner that meets or exceeds the ethical, legal, commercial and public expectations that society has of business." This is a concept whereby companies encompass its voluntary contributions to a better society and a cleaner environment as an integral part of its missions.

ROLE OF BUSINESS IN SOCIETY

Expanding global business operations, is shaping relations and deepening interdependencies between states, cultures and people. Economic openness and advancements in technology, science and communications have resulted into the globalization which further led to a fundamental shift in the pattern of economic activities and the corresponding opportunities. Due to the expanding pace of business, with staunch universal principles, the global market place has become a platform for creating more robust and even-handed markets. Superintend business practices will be instituting an advancement of international co-operation and development by including the social obligations along with economic considerations.

The contribution of business to society is multi-faceted from creating employment, ensuring income, enhancing technical skills, providing social benefits, strengthening the management and to bring focused market based solutions to any pressing environmental issues. Accountable and enterprising business practices respect human rights and ensure a clean and non-hazardous workplace environments, position itself towards environmental protection and cornerstone on a good corporate governance in order to create a tenable value and benefits for the entire shareholders. The business which professionally stands to manage the risks and opportunities would always places a premium in their overall valuation by connecting increasingly to the environmental and social performances.

Entities are assumed to be responsible socially due to the anticipated benefits from their actions. The benefits include, strengthening , beefed up corporate image, and an enticing domain for qualitative workforces. Of course, to have a stupendous economic growth will be on the top of the priorities for any corporates the above action will take the business close to its objectives. As higher costs are always associated with the any social obligations of the business, it is presumed that corresponding benefits arising due to the same will get offset against the related costs, but still the CSR of the business is indispensable in the current world.

FRAUD RISK – A GREATER CHALLENGE TO BUSINESS

Recent developments in the business world communicates invariably that the extent of fraud risk has increased multifold and has hit many businesses from various angles, the rationale behind the same are many.

Effect of Globalization:

As many organizations expand leaps and bounds in order to explore new sources for their inputs and to swell their sales in all potential markets, they may run across complex and surprising risks of fraud for which they may not have gird one's loins. These risks factors could range from bribery and corruption, to compliance with respect to product quality that can jeopardize customers. Enforcement by the Indian Agencies like Anti Corruption Bureaus, CBI in light of Indian Prevention of Corruption Act (IPCA), 1988, Prevention of Money Laundering Act, 2002 (PML Act) and by U.S. Department of Justice of the Foreign Corrupt Practices Act (FCPA) has also increased dramatically. Though all the above pressures are directing the business corporations to manage the financial, regulatory, and reputational risks associated with fraud and corruption, but still the same has a cascading effect on the operations.

Economic Slowdown:

The economy slowdown which is being witnessed currently are putting the business executives in to a difficult funnel whereby they literarily strive hard to achieve the plans. Such a scenario will be pushing more employees into a personalized financial crunch. Fraud examiners are of the opinion that the above pressurized conditions will be increasing the chances of frauds initiated by the individuals, may it be those who are in the regular course of employment or management officials, for the sake of achieving the corporate objects or personal needs. These actions invariably will be funneling additional cost burdens related to Frauds on the organization's financials which at the end of the day, the business will hardly be able to absorb.

Surprises related to the Risk Management activities:

Many recent instances in the business world send the market a clear communication that entities with sophisticated risk management processes are also facing the vulnerability of Fraud. It is not that there is lack of legal frame work in containing fraud.ⁱ Although Even the technology has aided the business to run the operations very effectively and has cut a path way towards better fraud management and monitoring activities, the complexity in terms such technological advancements have exposed the business houses to Fraud risks.

The new legal and statutory guidance's emphasize on the need that the Board of Directors of an organization along with the other governing body if any shall have to ensure that the corporate governance practices which highlights the corporate responsibility towards the society must be setting a tone for the effective management of Fraud Risks in the business entities.

LEGAL ASPECTS RELATING TO CSR AND FRAUD

CSR has been made mandatory by virtue of Companies Act, 2013. Corporate Social Responsibility is not limited to projects or programs related to activities which are specified in Schedule VII of The Companies Act, 2013. CSR provisions applies to every company, its holding and subsidiary company and foreign company having, in the preceding financial year, net worth greater than 500 Crore or turn over greater than 1000 crore or net profit greater than 5 crore. Board of Directors has a prominent role to play as far as implementation of CSR policy is concerned.ⁱⁱ The Board also has to ensure that company spends in every financial year a minimum of 2% of average net profits made during the three immediately preceding financial years as per the CSR Policy. If the CSR funding do not meet the 2% criteria, the non-spent fund shall be transferred to the specified fund. This has to be disclosed in the Board's Report. Thus Corporate manager's act as moral agents in determining the activities related to CSR. CSR activities improve the public image of the company by publicizing the efforts towards better society and disseminates the rays of positivity on the organization.ⁱⁱⁱ As ethical values of the corporate managers are reflected in their CSR activities, it is expected that likelihood and severity of corporate frauds would be reduced.^{iv}

In fact the new companies Act 2013 seeks to strengthen the shareholders action against the company for the fraudulent acts perpetrated by its employees. The Companies Act, 2013, provides that “If in any return, report, certificate, financial statement, prospectus, statement or other document required by, or for, the purposes of any of the provisions of this Act or the rules made thereunder, any person makes a statement,— (a) which is false in any material particulars, knowing it to be false; or (b) which omits any material fact, knowing it to be material, he shall be liable under section 447.”^vThe act also penalizes the person who commits fraud with imprisonment. ^{vi} For the purpose of the Act, the term fraud^{vii}in relation to affairs of a company or anybody corporate, was defined as to “include any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss”^{viii}The act also penalizes repeated defaults.^{ix} Apart from these, the act also penalizes the action of giving false information or suppressing material information, ^x misstatement in prospectus, ^{xi} fraudulently inducing persons to invest money,^{xii}issuance of duplicate certificate of shares. ^{xiii}The act also imposes liability on the persons in charge of the governance of the company, by making them liable if application is made for the removal of name from the register with the object of evading liabilities or deceiving or defrauding creditors.^{xiv} In order to ensure accountability and transparency and compliance with law governing corporate governance, Companies Act provides for vigil mechanism, ^{xv} to report genuine concerns of their grievances, risk management policy, ^{xvi} establishment of serious fraud investigation office, ^{xvii} reporting by auditors,^{xviii}appointment of independent directors.^{xix} Thus it can be seen that Companies Act has provided several duties and obligation on Board of Directors and individual members, the objective of which is to ensure transparency, accountability and to contain fraudulent and corrupt corporate activities. Thus several legal provisions and mechanisms has been envisaged by The Companies Act, 2013 so as to prevent and contain corporate frauds.

Prevention of Corruption Act also seeks to combat corporate frauds and corruption. As per Prevention of Corruption Act, ^{xx}if any person associated with a commercial organization gives or promises to give or promises to give undue advantage to a public servant he is liable to be

prosecuted. Personal liability is also imposed on such director or directors, who has consented or colluded to commit any offence. The requirement of mandatory disclosure of any political contribution in profit and loss account of the company by the Companies Act, 2013 also has its objective to prevent corruption and fraudulent activities.^{xxi} Apart from that Competition Act, 2002 tries to compact anti-competitive practices, which may also lead to corrupt practices.^{xxii} It is noteworthy that Indian Penal Code 1865 also punishes corporate frauds by penalizing cheating, concealment, forgery, falsification of accounts, criminal misappropriation and criminal breach of trust. It is submitted that apart from the above mentioned provisions, mandatory provision relating to corporate social responsibility also seek to contain fraudulent corporate behavior and promote ethical behavior in corporate governance.

CONCLUSION & SUGGESTIONS

There is no lack of legislative and regulative framework to promote ethical behavior among corporate managers. However, the Top Management should be initiating for the implementation of full-bodied policies encompassing the corporate social responsibility to augment the ethical behavior to bring down the fraud risks to naught. The roles and responsibilities for personnel at all levels of the organization whose respective objectives are aligned towards attaining the ultimate corporate objective ought to be defined distinctly to manage the Fraud Risks. These steps only will be elevating a business entity as a socially responsible operator whereby the null fraud risks will be yielding higher productivity and persistency in terms of quality of earnings.

Companies have to implement compliance programs, manuals etc to ensure that their employees are adequately been made aware with respect to regulatory legislations related to the Corporate Social Responsibilities and Fraud Risks. Trainings must be an HR integrated activity, whereby the new entrants are educated regarding the organizational policies and the existing employees are continuously being updated of the changes happening with respect to the legal frameworks. These initiatives to a great extent will bring down the fraud risks to an acceptable level.

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ENDNOTES

ⁱ There are provisions in Indian Penal Code, Indian Contract Act, Prevention of Corruption Act, Prevention of Money Laundering Act and Company's Act, which requires corporate managers to act towards prevention, detection, investigation and detecting of fraud.

ⁱⁱ Board of Director have to approve the CSR policy after considering the recommendations of CSR committee. The Board has to ensure that only those activities which are mentioned in the policy is undertaken by the company. The Board also has to ensure that company spends in every financial year a minimum of 2% of average net profits made during the three immediately preceding Financial years as per the CSR Policy. If the CSR funding do not meet the 2% criteria, the non spent fund shall be transferred to the specified fund. This has to be disclosed in the Board's Report.

ⁱⁱⁱ Kalidas, *Legal Provisions Relating to Corporate Social Responsibility- Some unanswered questions Still*, (Dec 2, 2014), <https://www.lawyersclubindia.com/articles/legal-provisions-relating-to-corporate-social-responsibility-some-unanswered-questions-still-6440.asp>

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^v The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 448.

^{vi} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 447 Any person who is found to be guilty of fraud, shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud: Where the fraud in question involves public interest, the term of imprisonment shall not be less than three years.

^{vii} The term fraud is defined in Indian Contract Act 1872 Section 17 as follows. "Fraud" means and includes any of the following acts: (1) the suggestion as a fact, of that which is not true, by one who does not believe it to be true; (2) the active concealment of a fact by one having knowledge or belief of the fact; (3) a promise made without any intention of performing it; (4) any other act fitted to deceive; (5) any such act or omission as the law specially declares to be fraudulent.

^{viii} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Explanation (i) to Sec. 447 defines as "wrongful gain" means the gain by unlawful means of property to which the person gaining is not legally entitled; (iii) "wrongful loss" means the loss by unlawful means of property to which the person losing is legally entitled. The terms are defined in Indian Penal Code also in the same lines.

^{ix} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 451. Provides for punishment in case of repeated default If a company or an officer of a company commits an offence punishable either with fine or with imprisonment and where the same offence is committed for the second or subsequent occasions within a period of three years, then that company and every officer thereof who is in default shall be punishable with twice the amount of fine for such offence in addition to any imprisonment provided for that offence. This section is not applicable to the offence repeated after a period of three years from the commitment of first offence.

^x The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 7(5)

^{xi} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 8

^{xii} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 36

^{xiii} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 46(5)

^{xiv} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 251

^{xv} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 177

^{xvi} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 134(3) The presence of a comprehensive policy may beseen to demonstrate bona fides of a company. Inthe event of any investigation or prosecution, A company may be able to demonstrate that it did what was reasonably possible by sensitizing employees, having

workshops and even a compliance audit to ensure that employees across the company, were aware of rights, obligations and duties under the law and in respect of business transactions. Such measures must however be aggressively and continuously monitored, updated and implemented

^{xvii} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec. 211 of the Companies Act empower the Central Government to establish an office called Serious Fraud Investigation Office ('SFIO') to investigate frauds relating to companies

^{xviii} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 143 of the Act, the Central Government requires the Auditor(s) of the Company to maintain transparency and as well as the interests of shareholders at large. Section 143 (12) read with Section 143(15) of the Companies Act and its Rules require an auditor of a company including branch auditor, cost accountant and company secretary in practice to report immediately to the Central Government in the course of the performance of their respective duties has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company.

^{xix} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 149 (6) makes a special provision for appointment of 'Independent Director' Section 149 also provides that the Independent Directors should abide Code for independent Directors as specified in Schedule IV of Companies Act ('Code'). The Code states the duties and responsibilities of Independent Directors towards the company and shareholders and stakeholders. Among all corporate governance duties, an Independent Director is also required to report the concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct or ethics policy

^{xx} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 29

^{xxi} The Companies Act 2013 No. 18. Acts of Parliament, (2013) Sec 182 there must be a resolution passed at a Board of Directors meeting authorizing such contribution under Section 182 (1) of the Companies Act. The penalty for non-compliance with a provision of the section which could be 5 times the amount so contributed and each officer of the company would be punishable with imprisonment for a term of 6 months and a fine which could be 5 times the amount contributed.

^{xxii} *An Overview of Anticorruption Laws in India- A Legal, Regulatory, Tax and Strategic Perspective*, Nishith Desai Associates (Mar 2020) http://www.nishithdesai.com/fileadmin/user_upload/pdfs/Research_Papers/Overview-of-Anti-Corruption-Laws-in-India-Web1.pdf