ISSN Print: 2394-7500
ISSN Online: 2394-5869
Impact Factor: 5.2
IJAR 2016; 2(11): 193-196
www.allresearchjournal.com
Received: 28-09-2016
Accepted: 30-10-2016

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Relation between corporate governance and corporate social responsibility: A review article

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Abstract
Both Corporate Governance and Corporate Social Responsibility have gained importance, specially, in the back drops of a number of corporate scams and scandals all over the world. Many laws and rules and regulations have been framed to ensure good governance and incorporate a sense of CSR in the activities of the companies. In India, Clause 49 of the Listing Agreement relates to Corporate Governance. Provisions related to Corporate Governance and CSR have been included in Companies Act, 2013. Review of Literature on CG and CSR have suggested that companies give due importance to both. Review of the studies undertaken on the topic suggests that there is a close relationship between the principles of Corporate Governance and Corporate Social Responsibility and both are required to be incorporated in the affairs of the company for its long term sustainability.

Keywords: Corporate Governance, Corporate Social Responsibility, Stakeholders, Sustainability

Introduction
Indian corporate sector has been in transforming phase from the last couple of decades. Economic reforms adopted in 1991 have truly enhanced the pace of this transformation. We see an increase in giant MNCs coming from all over the world and a huge increase in the scale of operations of their Indian counterparts. The competition has become intense among the corporate. In the era of cut throat competition in corporate sector, the interested of the stakeholders is at stake. The business draws various benefits from the society. The factors of production like man, material, money, land, etc. are provided by the society and the output (goods or services) are again consumed by the society. Thus, this fact can not be denied that business is amongst the constituents of the society and depends completely upon it for its survival. This interdependence of the business and society on each other makes the business answerable to various stakeholders. These stakeholders are consumers, employees, suppliers, competitors, government and society in general. The interests of various stakeholders are generally conflicting. The corporate sector is generally criticized for ignoring the interest of stakeholders while making the profits. A large number of corporate scams and scandals in India like Satyam, Speak Asia**,** Saradha Chit Fund etc. have put a lot of pressure on corporate for a better Corporate Governance. Better governance requires high degree of professionalism, vigilant role of directors, transparency in operations and disclosures, fairness in accounting and reporting, and fixing accountabilities, etc. However, during the process the aspect of Corporate Social Responsibility has also gained its importance. Corporate social responsibility is the responsibility o the business towards the stakeholders who are affected by it directly or indirectly. The growing importance of corporate social responsibility has lead to the introduction of provisions regarding it in the Companies Act, 2013. Now in India CSR is no more a voluntary activity but a legal obligation. In the present paper an effort has been made to underline the importance of CSR and Corporate Governance.

Corporate Governance
A company, despite of being a separate legal entity, is a congregation of various interest groups, called stakeholders. Being fair and transparent with respect to its all transaction by the stakeholders is the prime obligation of the company. It may not be able to succeed, if it doesn’t demonstrate an ethical conduct.

In the present era of increasing cases of misconducts and malpractices by companies, there is demand from the different sections of the society for the adoption of good Corporate Governance by the corporations. Corporate Governance is about ethical conduct about the business. In other words it is the ethical framework adopted by the corporations within which various corporate decisions are taken. Generally, Corporate Governance is defined as a system through which corporate entities are directed and controlled. It implies to put in place a system of checks and balances between the shareholders, directors, auditors, management and the society. It refers to a set of rules that are designed to govern the behavior of corporate enterprises. CG aims to redefine business goals in such a manner that business becomes socially more relevant. CG is needed to create a corporate culture of social consciousness and openness. Although the idea of CG has received a wide attention, there is a considerable variation in the conceptual definition, in its narrower sense the term may be described as a formal system of accountability of senior management to the shareholders and in the wider sense the term is stretched to include the entire network of formal and informal relations involving the corporate sector and their consequences for the society in general. Corporate Governance, however, as generally understood, includes the structure, process, cultures, and systems that engender the successful operation of the organization. According to Chandratre (1997) [6] "corporate governance is a broad and somewhat vague term used to refer to a range of corporate control and accountability mechanisms designed to meet the aims of corporate stakeholders." Narang (1997) [14] defined CG as direction and control of the affairs of the company. In India Corporate Governance became mandatory when the clause 49 of the Listing agreement was introduced. All the companies listed on stock exchanges have to comply with the provisions of clause 49. To address certain issue related to Corporate Governance, Ministry of Corporate Affairs also issued some voluntary guidelines applicable to companies. Now, when provisions regarding corporate governance have been included in Companies Act, 2013, Security and Exchange Board of India has also amended its Listing Agreement to get aligned with the new Companies Act. The key changes in provisions regarding corporate governance in Companies Act relate to composition of board, board committees, board meetings and processes, etc.

Thus, Corporate Governance is concerned with establishing a system whereby directors are entrusted with responsibilities and duties in relation to the directions of a company's affairs. Corporate Governance is also concerned with the ethics, values and morals of a company and its directors. Accountability, fairness, and transparency are considered as fundamental principles of Corporate Governance, which ensure a company's integrity and competence. A company with good Corporate Governance will provide more value addition to their stakeholders, whereas, stakeholders of a poorly governed company may end up losing their respective 'stakes'. Thus, good Corporate Governance will ensure a company's better future which will lead to its contributions towards the society and economy.

CSR

Corporate Social Responsibility refers to the obligations of business to pursue such policies, to make such decisions, and to follow such practices, which are desirable in terms of the increased welfare of the stakeholders. Thus, CSR may be defined as the obligations of companies to protect and enhance the values hold by the society within which it operates. As defined by the World Business Council for Sustainable development, "Corporate Social Responsibility is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large". Although profit is the major determining factor, business in now making an effort to strike a meaningful balance between conflicting needs of earning profit and society's needs by catering to consumers, employees, Govt. etc. Business is an economic activity to earn profit for the owners an social responsibility means serving community without any expectations. According to Dr. Sushma Bareja (2005) [2], there are two pivotal features of CSR. These are:

1. An action must be voluntary to qualify as a socially responsible action i.e. it should be carried out voluntarily without any govt. coercion. Any activity or programme adopted under legal compulsion should not be considered as a social; programme. The company is expected to do a social activity over and above any legal enforcement in order to improve its social image
2. There should be emphasis on means rather than ends i.e. the company should incorporate into its decision making process the means by which social concerns will be given full consideration.

Now the question arises why is there a need for a business to serve the community? Business is expected to create wealth, create markets, generate employment, innovate, and produce sufficient surplus to sustain its activities and to improve its competitiveness. Society is expected to provide an environment in which business can develop and prosper, allowing investors to earn returns. So the business enterprise, which makes use of the resources of the society and depends on it for its functioning, should contribute to enhance the welfare of the society. Introduction of New Companies Act has now changed the way the corporate practices CSR in India. It mandatory now to comply with CSR related provisions included in the Companies Act. These provision are applicable to the companies having net worth of Rs 500 crore or more; or turnover of Rs 1000 crore or more; or Net profit of Rs 5 crore or more during any financial year. The companies falling within the above criteria are required to constitute a Corporate Social Responsibility Committee of the Board comprising of three or more directors. At least one director comprising the committee shall be an independent director. These companies are required to spend at least 2% of their average net profit in the previous three years on CSR activities. Net profit for this purpose would be the profit before tax as per the books of accounts, excluding profits arising from branches outside India. New Companies Act has also specified some areas, which will be considered as CSR activities.

CG and CSR: Relationship

Now question arise how CG is related to CSR? From CSR point of view organizations should have ethical and moral values and policies are to be framed with such values. Such values always strengthen the thinking and ideologies of corporate managers and in turn they further lay their strength to such core values, which in turn enables a good corporate governance. Sudhakar (1998) [17] says that good corporate governance comprise of certain responsibilities by the corporate. These are towards the shareholders who are the ultimate owner of the company, towards the customers, suppliers, government, the society and last but not the least, towards the employees. Bhimani and Soonawalla (2005) [5] also suggested that CG and CSR are two sides of the same coin. Arora and Dharwadkar (2011) [1] found that impact of corporate governance on positive CSR is more pronounced under low slack/negative attainment discrepancy conditions, and that on negative CSR is more pronounced under high slack/positive attainment discrepancy conditions. Here is the brief discussion of how we relate the Corporate Governance Corporate and Social Responsibility towards various stakeholders.

Shareholders

Handling shareholders' grievance is very important. To get the grievance settled, they have to have long corresponds with the company and has to run around the authorities. So communication between the shareholders and company is very important. At the general meeting of the companies they have to be provided with an opportunity to know about the company's performance and the future plans. Ruangviset *et al*. (2014) [15] stated that while enhancing shareholder value is still a major goal for all company, the concepts of corporate governance (CG) and corporate social responsibility (CSR) enter the picture to reach to the goal.

Customers

It is the customers who provide opportunity to the companies to do business. They are to be provided with quality products, good after sale services at minimal profit. Everyone knows that companies are not charitable institutions and they do business with a profit motto. However, the essence of good corporate governance is to perform under competitive environment with fair trade practices, strictly adhering to the business ethics.

Government

Compliance with rules and regulations, timely payment of duties and taxes, submission of return are part of good Corporate Governance. Organisations must realize that they can not become profitable by tax evasion or breaking laws. Tax planning is a part of good Corporate Governance but not tax evasion.

Society

Organisations have to realize their duties towards society. They should not cause pollution and have to keep the environment clean. Responsibilities towards society must be the part of Corporate Governance. Kolk (2008) [11] examined to what extent and how current sustainability reporting of Fortune Global 250 companies incorporates corporate governance aspects. It was concluded that many multinationals, particularly in Europe and Japan, have started to pay attention to board supervision and structuring of sustainability responsibilities, to compliance, ethics and external verification. While detailed disclosures are not yet common, some notable practices can be found.

Employees

Employees have to be given ample scope to perform and achieve. They are to be encouraged and their growth is to be ensured. Their emotions and sentiments are to be respected.

A number of studies have been undertaken on the relation and importance of Corporate Governance and Social Responsibility. Findings and results of some of the studies have been discussed in the following review section.

Dr. Shushma Bareja (2005) [2] also highlighted the importance of corporate social responsibility in corporate governance. She says that codes of Corporate Governance like UN Global Impact and OECD guidelines for multinational enterprises also want their corporations to be socially responsible. The Department of Company Affairs appointed a study group in 2002 under the chairmanship of Dr. Sanjeeva Reddy, then Secretary, DCA, to suggest new norms for better CG. One of the key recommendations of the study group was "introducing formal recognition of CSR with Triple-Bottom line Accounting and Reporting". Even SEBI's Kumar Mangalam Committee report has also highlighted the fact that Corporate Governance is about ethical conduct in business. CG deals with conducting the business of a company such that there is a fairness to all the stakeholders and its actions benefit the greater numbers of stakeholders. The social approval to the existence of a corporate entity as a responsible corporate citizen arises from the public confidence and public confidence can be raised and maintained only with better Corporate Governance. The Turnbull Report, providing guidance on the Combined Code on Corporate Governance, recommends company boards should focus and manage the full range of risks including; health, safety, environment and reputation. The Dow Jones Sustainability Index is launched in the US. The index is restricted to companies that are committed to "green" technologies and good corporate governance. The index provides objective benchmarks to asset managers to manage sustainability portfolios.

According to Beltratti (2005) [4] Corporate Governance and Corporate Social Responsibility are complementary in their shaping of the objective function and the constraints faced by corporations. They can reinforce each other in the modern vision of the firm as an institution that does not disregard various relevant constituencies in its search for increases in value. Maier (2005) [13] defined scope of CG as a set of relationships between a company's management, its board, its shareholders and its stakeholders. It is the process by which directors and auditors manage their responsibilities towards shareholders and wider company stakeholders. For shareholders it can provide increased confidence of an equitable return on their investment. For company stakeholders it can provide an assurance that the company manages its impact on society and the environment in a responsible manner. Shahin and Zairi (2007) [16] found that Corporate Governance encompasses different internal and external factors, by which management of organizations are influenced. The leadership style is also found to play an important role in socially responsible organizations. In this respect, transformational leader seems to be more effective, compared with manager and transactional leader. The paper suggests that organizations should audit their CG capabilities towards CSR, based on a proposed questionnaire in order to drive excellence in CSR. Based on an analysis of CSR reporting of Fortune Global 250 companies, findings show that more than half of them have a separate corporate governance section in their CSR report and/or explicitly link corporate governance and CSR issues. Jones *et al*. (2007) [8] stated that The European Union promoted CSR in all member states and the European Commission argues that CSR has gained increasing recognition amongst companies as an important element in new and merging forms of governance because it helps them to respond to fundamental changes in the overall business environment. It was further stated that the majority of the top ten global retailers have been keen to recognise, and report on, some of the impacts that their businesses have on the environment, the economy and society and a number of them claim to be committed to integrating CSR agendas into to their core business activities and governance frameworks. Jamali *et al*. (2008) [7] concluded that CG and CSR should not be considered and sustained independently. Irrespective of the type of relationship that exists between CG and CSR, a company without an efficient long-term view of leadership, effective internal control mechanisms, and a strong sense of responsibility vis-à-vis internal stakeholders cannot possibly pursue genuine CSR. Conversely, CG is not entirely effective without a sustainable CSR drive because a company has to respond to the needs of its various stakeholders in order to be profitable and create value for its shareholders/owners. Khan (2010) [10] stated that nowadays consciousness for CG has not only been increased but the concept has greatly been widened. For example, it has started to envelop some areas customarily perceived as being part of CSR.

According to Barthorpe (2010) [3], CSR could be considered as an “umbrella” term, incorporating the tenets of; environmental sustainability, business ethics, governance, public relations, stakeholder analysis and relationship marketing. Khan *et al*. (2013) [9] suggested that pressures exerted by external stakeholder groups and corporate governance mechanisms involving independent outsiders may allay some concerns relating to family influence on CSR disclosure practices. The study implied that corporate governance attributes play a vital role in ensuring organisational legitimacy through CSR disclosures.

Conclusion

Review of the studies undertaken on the topic suggests that there is a close relationship between the principles of Corporate Governance and Corporate Social Responsibility and both are required to be incorporated in the affairs of the company for its long term sustainability. Introduction of provisions related to corporate Governance and Corporate Social Responsibility in the Companies Act, 2013 has increased the importance of both in India. It can be concluded that fulfillment of CSR is a great managerial skill required for better CG. Corporate Governance can be converted into good governance while maximising the value for shareholders, customers, employees, government and the general public. Thus, Corporate Social Responsibility can be used as one of the important tools for Corporate Governance. A proactive approach by the management towards CSR is always helpful in protecting the interests of the stakeholders and ultimately leads to sustainability.

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