CORPORATE GOVERNANCE: COMPARATIVE ANALYSIS BETWEEN INDIA AND USA

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ABSTRACT

The "corporate governance concept" dwells in India from the Arthshastra time instead of CEO at that time there were kings and subjects. Today, corporate managers and shareholders replace them but the principles still remain the same, unchanged i.e. good governance. While in the India the discussion on corporate governance can be dated back to the birth of East India Company, realization of its importance came in the second half of 1996 where economic liberalization and deregulation of companies started. Since the government no longer had full control over the companies, the need for corporate governance hence the accountability and good management increased. It was in 20th century that India finally became a full-fledged part of the global market due to liberalization, globalization and privatization. On the other hand, the term became much more prevalent in United States from 1970's onwards. "Corporate Governance" first appeared in the Federal Register in 1976, when the Securities and Exchange Commission brought up the topic. This was after world war 2 when companies were flourishing in the United States. After the financial crisis of 2007, the concept and application of corporate governance received stringency. The collapse of Lehman Brothers bank led to the realization and importance of greater accountability from the company's board and shareholders. This paper aims to look at the United States of America and India, their approaches regarding corporate governance and how the difference in their legal, culture and regulatory environment has an impact on their company's management structure.

CORPORATE GOVERNANCE: COMPARATIVE ANALYSIS BETWEEN INDIA AND USA

Research Question: Does the legal and regulatory environment of a country has an impact on its corporate governance model?

Introduction

In common parlance, "Corporate Governance" means a set of system, principles and processes along with the relationship the company's board has with its shareholders, creditors and other stakeholders. An academician would define it as 'the control of management in the best interests of the company, including accountability to shareholders who elect directors and auditors and vote on say on pay. How a company is governed influences rights and relationships among organizational stakeholders, and ultimately how an organization is managed, and whether it succeeds or fails. Companies do not fail: boards do.' (Dr. Richard Leblanc, Harvard University Summer 2015)[1].

Legally it can be defined as something concerned with holding the balance between economic and social goals and between individual and communal goals. The corporate governance framework is there to encourage the efficient use of resources and equally to require accountability for the

[1] James McRitchie, "Corporate Governance Definition", https://www.corpgov.net/library/corporate-governance-defined/ <Accessed 3 March 2020>

stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society.[2] Good corporate governance helps to build an environment of trust, transparency and accountability necessary for fostering long-term investment, financial stability and business integrity, thereby supporting stronger growth and more inclusive societies.[3] Based on corporate developments in the last few decades, certain theories of corporate governance emerged such as agency, stakeholder, resource dependency, stewardship, Transaction cost and political, through which the trajectory of corporate governance and the challenges faced can be understood.

AGENCY THEORY

Agency theory, expanded by Jensen and Meckling, fundamentally defines the relationship between managers and shareholders. In this, the principals of the company i.e. shareholders hire agents i.e. managers to work. According to this theory, shareholders expect the agents to act and make decisions in the principal's interest. On the contrary, the agents may have interests which do not align with those of the principals and hence not necessarily make decisions in the best interests of the principals.[4] The underlying assumption of this theory is that agents may be guided by self-interest rather and may take advantage of the power given to them by the principals, in order to further their own well-being. Further, a manager cannot always act in the interest of the shareholders, situations may come up when their interest differs from those of the shareholder's, this happens due to separation of ownership and control, where the ownership lies with the principals i.e. the shareholders. This conflict is an agency problem. Then the best solution would be in form of controls for the managers' actions-hence it is likely that agency conflicts and governance mechanisms are complementary.[5] So, importance of agency theory comes from the fact it helps provide clear guidelines in the way that managers should act while making strategic decisions. This also helps limit them to use their power to the disadvantage of the principals.

STEWARDSHIP THEORY

The stewardship theory, also known as the trusteeship theory, was introduced by Donaldson and Davis as an alternative visualisation to the Agency Theory. This theory recognizes that there is some form of agency present in a corporate environment but it deems that the managers/agents act as stewards for the best interest of the company and their actions will be driven towards the end goal of the organization as a whole. This is in opposition of the assumption on which the agency theory is based (where agents are not trustworthy). This theory relies on the trust between the principal and the steward and assumes that both their interests are aligned. So, stewards are motivated by intrinsic rewards like trust, enhancement of reputation, discretion and autonomy, level of responsibility, stability, and mission

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[2] *Ibid.*

[3] "Corporate Governance", http://www.oecd.org/corporate/ <Accessed 3 March 2020>

[4] Haslinda Abdullah, Benedict Valentine, "Fundamental and ethics theory of Corporate Governance", *Middle Eastern finance and economics*, vol. 9, no. 4 <Accessed 1 March 2020>

[5] Aiyesha Dey. "Corporate Governance and Agency Conflicts." *Journal of Accounting Research*, vol. 46, no. 5, 2008, pp. 1143–1181. *JSTOR*, www.jstor.org/stable/40058121. <Accessed 3 March 2020>

alignment.[6] The goals to be achieved by the owners and managers are collective goals. Hence, the autonomy given to a steward should be extended so that the benefits reaped by the pro-organizational behaviour of the steward are maximized.[7] So, auditing and financial reporting would be methods which would work well and similarly, presence of outside directors are likely to hinder their progress.

TRANSACTION COST THEORY

Transaction cost theory, put forward by Ronald Coase, is based on the principle that there are various costs that will arise as a result of an agency relationship. It interprets governance frameworks as a result of transactions – internal and external. This means that, focus is put on the economics of transactions, and where there are transactions, there will likely be contracts which will bind the company to its fulfilment. It suggests that directors on an average level, prefer being tied into deals as that will reduce their stress levels as well as save time and expense that may be spent in renegotiation or negotiating new deals. But this may also cause them to lose the flexibility that they might have had in the absence of a long lasting contract. The theory emphasizes on the corporation as an efficient hierarchy that is structured to enable contractual relationships. The transaction cost theory also considers the costs that arise from the conflict of interest between managers and shareholders; this includes the cost of using the agent as well as the money spent on protectionary measures against agent's opportunistic behavior.

RESOURCE DEPENDENCY THEORY

The theory first emerged in 1970 with the publication of 'The External Control of Organisation: A Resource Dependence Perspective', by Jeffrey Pfeffer and Gerald R. Salancik. This theory is mostly concerned with how organisational behaviour is affected by external resources the organisation utilises, such as raw materials. The theory is important because an organisation's ability to gather, alter and exploit raw materials faster than competitors can be fundamental to success.[8] The theoretical arguments that serve as RD's foundation can be summarized as follows: (1) an organization's external environment comprises other organizations, each with their own interests and objectives; (2) organizations hold power over a focal firm—and may thus constrain its behaviour—if they control resources that are vital to its ongoing operation and cannot be acquired elsewhere.[9]

STAKEHOLDER THEORY

This theory takes into consideration the effect of corporate action on the stakeholders of the company. Stakeholders can include internal stakeholder (Corporate

[6] David M. Van Slyke "Agents or Stewards: Using Theory to Understand the Government-Nonprofit Social Service Contracting Relationship." *Journal of Public Administration Research and Theory: J-PART*, vol. 17, no. 2, 2007, pp. 157–187. *JSTOR*, www.jstor.org/stable/4139740 <Accessed 3 March 2020>

[7] James H. Davis et al. "Toward a Stewardship Theory of Management." *The Academy of Management Review*, vol. 22, no. 1, 1997, pp. 20–47. *JSTOR*, www.jstor.org/stable/259223 <Accessed 3 March 2020>

[8] 'What is resource Dependency Theory', https://www.hrzone.com/hr-glossary/what-is-resource-dependence-theory-rdt , <Accessed 3 March 2020>

[9] Adam Cobb and Tyler Wry, "Resource Dependency Theory", *Oxford University Press*, (June 2014) <Accessed 1 March 2020>

employees and directors) and external stakeholder (Creditors, auditors and customers). The main posit of the theory is that the managers should take into consideration the interests of the stakeholders into account before making any decisions. Freeman (1984) contends that the network of relationships with many groups can affect decision making processes as stakeholder theory is concerned with the nature of these relationships in terms of both processes and outcomes for the firm and its stakeholders. Donaldson & Preston (1995) argued that this theory focuses on managerial decision making and interests of all stakeholders have intrinsic value, and no sets of interests is assumed to dominate the others.[10]

POLITICAL THEORY

Political theory talks about allocating the organisations' corporate power, profits and powers are determined via the government's favour. This theory tends to explain corporate governance through legal and political influence in the company. Politics of organizing financial institutions affects the flow of capital into the large firm and, hence, the power and authority of shareholder-owners. Managers wield considerable political influence, which they use to shape the rules governing corporate finance and capital markets. [11]

CORPORATE GOVERNANCE SCANDAL IN USA AND INDIA

Before discussing the ideal corporate governance model as well as model that exists in the two countries, it is pertinent to examine the failure both the companies has faced in the past when lack of proper corporate governance strategies and faced the consequences therein. To do this the classic case of Enron Scandal in USA and Satyam Sandal in India can be referred to.

ENRON SCANDAL

Enron was an energy company founded by Kenneth Lay. In the year 2000, it was very attractive to the investors and was thought of as world's leader in business like Apple and Google but better. It was making money and growing at a rate that no one has seen before. The company generated multi-billion dollar revenues. The Enron employees made it clear that the company will grow further supports the claims with low debts as compared to high equity. However, immediately after one year in 2001, the stock did not go up. The stock that were valued at 80-90 went down to 50-60 cents. Thousands of people including the Enron employees who had invested in retirement plans that were tied in the stock and lost all the money. Enron declared itself bankrupt in December 2001 leading to loss of jobs and money.

As it turns out, the numbers that Enron had provided the public were all from cooked books and were fake. They had just projected those earning using the mark to market accounting method, after the contract with blockbuster, which failed drastically. They also hid the debt by transferring it to SPV. The CEO of the company, Jefferey Skilling, used to hire accounts to do poor

[10] Haslinda Abdullah, Benedict Valentine, "Fundamental and ethics theory of Corporate Governance", *Middle Eastern finance and economics*, vol. 9, no. 4 <Accessed 1 March 2020>

[11] Mark J. Roe and Massimiliano Vatiero, "Corporate Governance and its Political Economy", *Harvard Law School* (April 2, 2015), http://www.law.harvard.edu/programs/olin_center/papers/pdf/Roe_827.pdf < Accessed 1 March 2020>

financial reporting to hide debt. The CFO, Andrew Fastow, used to mislead the board of directors and audit committee of financial issues. They managed the bankers, lawyers and the auditors as well. Arthur Anderson, the top most accounting firm, was fired to ignore the issues and were paid heavily to do that. After bankruptcy was filed, the stocks that were held by the employees were also not allowed to sell, but the people involved in the scandal, with the means of insider trading, sold their stocks at top prices and exited the company.

This case had huge impact on the shift of corporate governance model of United States. The ethical behaviour of people is a key ingredient in a perfect model of corporate governance which was clearly violated here. The Enron Case reveal problems of a number of parties involved in the company including dysfunctional corporate culture, greed of executives, incompetent board and unethical auditor. This turned out be a clear violation of the agency and stakeholder theory that we discussed earlier in the paper. It was after this company that US passed the Sarbanes Oxley Act 2002, through which the corporate executives took personal responsibility about the affairs of the company. This act introduced many laws included provision on independent directors and strict documentation requirements. Along with increasing protection for the whistle-blowers, the act provided independence and financial literacy to the board[12]. A public company accounting oversight board provision is also included to mitigate any such risks in the future.

SATYAM SCANDAL

The Satyam Scandal, often called the 'Enron of India', is a corporate scandal involving a fraud of around $1.47 billon, with such a huge lapse in corporate governance, it substantially increased the need and importance of the same in India. Satyam Computer Services Limited was formed in 1987 by Ramalinga Raju, dealing in the IT industry and business process outsourcing services. The company started gaining success, went public in 1991 and got listed on Bombay and New York Stock Exchanges. It steadily grew to become one of the big four IT companies in India.

This success story however, was broken in 2008-2009 when Ramalinga Raju confessed to the huge fraud committed by him and his relatives. What had been happening was that as Satyam Computer Services Limited was doing well in the IT sector, Raju became interested in collecting real estate which became the reason for his committing fraud. When he needed more money to buy properties, he started manipulating the financial statements of Satyam Computer Services Limited by inflating the profits, showing more sales etc. It was later found out that this was done by faking sales invoices and substantiating the profits made out of these fake sales invoices through fake bank statements.

However, this was seen as fast growth of the company and share prices began to rise, meanwhile Raju started selling his shares in the company and used that money to buy more properties. The promotors of the

[12] Kimberly Amadeo, "Sarbanes Oxley summary" https://www.thebalance.com/sarbanes-oxley-act-of-2002-3306254 <Accessed 4 May 2020>

company also started selling their shares at this high price.

Raju had inside information due to which he bought certain properties thinking that the increase in the value of those properties would be used to cover the disparities in the financial statements shown and the actual figures. This had been happening since 2001 and the difference between the actual figures and fake figures rose substantially.

In 2008 there was a recession, causing Raju's plan to fail. He then proposed that Satyam would buy stakes in Maytas Infrastructure and Maytas Properties, the money would go to the promotors of Maytas and the gap in actual figures and fake figures would be used to buy these two companies. But there would not be any actual transfer of money since the two companies were owned by his family. The Board of Directors approved of this plan without the permission of the shareholders and the investors protested against this hence the stock price started decreasing rapidly. Due to the falling stock price, this plan was also cancelled. Soon after in January, 2009, Raju confessed.

Questions were raised on the activities of independent directors and the auditors of the company and it was found out that the auditors were paid double the amount than what was paid to other audit companies in the IT sector. Raju was then arrested, his properties were seized and along with his family members, they were banned to invest in the securities market for 14 years.

The Satyam Scandal clearly showed the gaps in the Indian Corporate Governance climate. Some of the actions include updating the Companies Act to include a wider range of activities with stricter requirements. SEBI increased the disclosure requirements of promotors and controlling shareholders and the scam also helped push India to adopt IFRS (international accounting standards).[13] One of the most blatant corporate governance mistake here was no separate splitting of roles as should be; Raju singlehandedly drove the entire fraud. The important thing is ethics which do not translate from person to person hence providing for it becomes necessary via stricter corporate governance controls. Satyam highlighted the cracks in the corporate governance mechanism of India by not being detected for such a long time.

CORPORATE GOVERNANCE IN INDIA

As stated earlier, corporate Governance has been much talked about in India particularly after 1993. Liberalization brought mixed results for Indian economy. It brought in its wake a spate of corporate scandals and later on many companies disappeared after making public issues with large premium. Primary markets collapsed and family owned businesses became corporate entities. The question, how to function in a corporate setup overriding family interest and obligations called for a code of governance. Auditors were also following questionable accounting practices on biggest of management and often advising doubtful accounting choices. All these factors put strong pressure on many corporates to Evolve a good governance practice.

[13] Madan Lal Bhasin, Corporate Accounting Fraud: A Case Study of Satyam Computers Limited *Open Journal of Accounting, 2013*, 2, 26-38. Available at SSRN: https://ssrn.com/abstract=2676467 < Accessed 4 May 2020>

Companies in India like Tata group, Infosys, Wipro have involved sound principle of governance, intertwining corporate governance with social responsibility. These companies in spite of being global companies also follow set standard norms regarding independent directors, meeting quality norms, rights of employees etc. It began in 1998 with the Desirable code of conduct[14], published by CII, committee formed in 1996. SEBI later formed two more committees, Kumar Manglan Birla and Naryan Murthy. All the committees are discussed herein.

CII REPORT

The Confederation of Indian industry took the initiative to draft some codes of corporate governance. National task force on corporate governance was set up in mid 1996 under the leadership of Mister Rahul Bajaj, ex-president, CII, and then CMD, Bajaj Auto limited. The committee issued desirable corporate governance. The major recommendations included, Board meetings at least six times a year, no person holding directorship in more than 10 companies, listed companies having more than 100 crore turnover and paid capital of at least 20 crore, must appoint ordered committee within 2 years. Board members Should be furnished with adequate information to discharge the duties. Non-executive directors should actively participate in board affairs and not be passive advisors and should be adequately paid. A compliance certificate signed by the CEO and CFO stating that management is responsible for preparation, integrity and fair presentation of financial statements and annual reports which suggest that company will continue in business. If the company does not conform to standard practices, full disclosure should be made in the audit report. Corporate governance guidelines - both mandated and voluntary - have evolved since 1998, thanks to the efforts of several committees appointed by the Ministry of Corporate Affairs (MCA) and the SEBI.[15]

KUMAR MANGALAM BIRLA COMMITTEE

Over the years, there were increasing concerns about Standards of financial reporting and accountability specially after losses suffered by investors and lenders which could have been avoided by better and more transparent reporting practices. There were concerns regarding following of standard shareholders' services. Thus, this committee was set up to address the new concerns.

This committee was set up in 1999, under Kumar Mangalam Birla, who was a member of the SEBI Board. The main aim of this committee[16] was to raise the standards of and promote good corporate governance. The recommendations that the committee came up with were divided into two parts- mandatory and non-mandatory.

The mandatory recommendations would apply to those listed companies which had a paid up share capital of 3 crore or more.

[14] The Desirable code of corporate governance, 1998. http://www.nfcg.in/UserFiles/ciicode.pdf <Accessed 9 May 2020>

[15] Corporate governance recommendation for voluntary adoption. https://www.cii.in/PolicyAdvocacyDetails.aspx?enc=BdcSgYOxVgzbSuwqN3yE86nEtIhzcYBE+kMrq8nUCmQ=

[16] Kumar Mangalam Birla Committee, 2000 http://www.nfcg.in/UserFiles/kumarmbirla1999.pdf <Accessed 9 May 2020>

Mandatory recommendations included having a combination of executive and non-executive directors in the board of directors, having 3 independent directors in the audit committee and that any information regarding investments of the shareholders should be shared to them. They also prescribed that a director should not be a part of more than 10 committees and act in the chairman's capacity for any more than 5 committees across the companies. The committee also recommended the amount of times the board should hold a meeting for reviewing budgets, quarterly results and plans- at least 4 each year with a maximum gap of 4 months between 2 meetings. Whereas the non-mandatory recommendations dealt with role of the chairman, corporate restructuring and further issue of capital and more.

NARAYAN MURTHY COMMITTEE

In its zest to improve governance in the companies through the regulatory processes SEBI also constituted committee the Narayan Murthy Committee. Set up in 2002, it focused its recommendations on role of auditors, the relationship of the company and the auditors and corporate audit. Mandatory recommendations[17] included strengthening the responsibilities if audit committees, improving the quality of financial disclosures which would include how the proceeds from initial public offerings were used as well as related party transactions. Emphasis on a whistle blower policy being placed was also made and responsibilities on the board were put to make, adopt and follow a formal code of conduct. Also discussed were the position of nominee directors and the fact that business risks should be disclosed in the annual reports of the companies. Non mandatory recommendations dealt with training of board members and peer evaluation of the non-executive director by all the board members

NARESH CHANDRA COMMITTEE[18]

On 21 August, 2002, The Department of company affairs under the Ministry of Finance and company affairs appointed committee under chairmanship or Sri Naresh Chandra to examine various corporate governance issues. The committee has been interested with analysing and recommending changes if necessary, in various areas, like, statutory auditor company relationship, independence of auditing functions, certification of account and financial statements by managers and directors, adequacy of regulation of Chartered Accountants, company secretaries, cost accountants and other similar statutory oversight functionaries, the role of independent directors, etc. The recommendations have also been drawn from the Sarbanes Oxley act, 2002, of the USA.

It is very clear after looking at all these committees, that the essence of corporate governance lies in transparency, integrity and Accountability of management, which also includes the non-executive directors. The main aim of corporate

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[17] Narayan Murthy Committee, 2003 https://www.sebi.gov.in/reports/reports/mar-2003/the-report-of-shri-n-r-narayana-murthy-committee-on-corporate-governance-for-public-comments-_12986.html <Accessed 9 May 2020>

[18] Naresh Chandra Committee, 2002 http://reports.mca.gov.in/Reports/3-Naresh%20Chandra%20committee%20report%20on%20regulation%20of%20private%20companies%20and%20partnerships,%202003.pdf <Accessed 9 May 2020>

governance is to handle corporate frauds and scandals, and it is a system of making directors accountable to shareholders for the effective management of the company and also with adequate concern for ethics and values. [19]

ROLE OF SEBI

In India, SEBI established in 1988 and was given stator power in 1992, as a regulator and watch dog has pivotal role and responsibility in enforcing corporate governance practices on corporate entities.[20] SEBI was setup in 1992 and since then has taken many steps to improve corporate governance in India and make it efficient. SEBI's initiatives usually aims to achieve the pillars of effective Corporate governance, like transparency, accountability, disclosure, equity and fairness. SEBI has taken initiatives to align Indian corporate governance practices with the global standards adopted in advanced economics.[21] SEBI set up various committees thereby establishing rules and laws and giving various recommendations on effective corporate governance.

To improve the corporate governance practices, SEBI amended Clause 49 of its Listing Rules, which came into effect in January 2006. This amendment was brought forward by the recommendation of the Narayan Murthy Committee and changes the various other committees recommended. Clause 49[22] would apply those companies which wanted to get listed for the first time and those companies which had a paid up share capital of 3 crore or more. It specifically laid down that company boards should lay down the code of conduct to be followed by the board members and the senior management of the company. Further, balance sheets, cash flow statements and profit and loss accounts should be certified by the chief executive and chief finance officer and that non-executive director's compensation was to be decided by the Board and approved by the shareholders.

Clause 49 was further amended[23] in 2013, to bring it up to date with the amendments made in the Companies Act, 2013. It now included provisions for having at least one woman director, it also laid down that no person can be a director in more than 7 listed companies at the same time, independent directors were also disentitled from any stock option, among other changes.

AMENDMENTS TO THE COMPANIES ACT, 1956

The SEBI did not have complete autonomy however, the authority in key areas remained with the department of Company Affairs (DCA). After the economic reforms programme that India undertook in 1990s it felt the need for a comprehensive review of Companies Act, 1956. After 3 unsuccessful

[19] Neetu Prakash, 'Role of SEBI in Corporate Governance (with special reference to Scams of Capital Market since 1991)' *SEBI and Corporate Laws* (January 25-31, 2010), p 29.

[20] Chaluvaiah, 'Role of SEBI as a regulator in maintaining corporate governance standards in India', *International Journal of Applied Research,* (2015) http://www.allresearchjournal.com/archives/2015/vol1issue13/PartB/2-11-88-373.pdf <Accessed 10 May 2020>

[21] *Ibid.*

[22] SEBI Circular No. SEBI/CFD/DIL/CG/1/2006/13/1 https://www.sebi.gov.in/legal/circulars/jan-2006/corporate-governance-in-listed-companies-clause-49-of-the-listing-agreement_14707.html <Accessed 10 May 2020>

[23] SEBI Circular No. CFD/POLICY CELL/2/2014 https://www.sebi.gov.in/sebi_data/attachdocs/1410777212906.pdf <Accessed 10 May 2020>

attempts in 2003, India decided to rewrite the company law. After almost 24 amendments later since 1956, there were various laws amended and added to improve the condition. Some of the amendments to the Companies Act which are remarkable and have a direct bearing on improvement in the standards of corporate governance are, passing of resolution by Postal ballot was to be conducted only by Postal ballot. After passing resolution through Postal ballot the company shall send notice to all shareholders by registered post. If the resolution requires majority or shareholders by means of Postal ballot it shall be deemed to have duly past a general meeting convened in that behalf. Under directors responsibility statement the both report shall into the directors responsibility statement. [24] Other amendments previously included, Additional powers and duties of auditors, Audit committee, Issue of shares with differential rights, buy back shares, liberalization of inter corporate loans and investment norms, etc.

CORPORATE GOVERNANCE IN USA

The system of corporate governance in USA went through a lot of changes to now be considered as largely a shareholder oriented one. Before the 1980s, the corporate era was characterized by strong managers and weak owners. The 1980s was characterized by a large amount of hostile takeovers, investors became more engaged in the corporate process, but by the 1990s, the managers re-established themselves by lobbying for stronger hostile takeover laws however, at the same time, they started recognising the importance and inclusion of shareholders.

The focal point of corporate governance in the USA comes from the Sarbanes-Oxley Act which was introduced by the Federal Government in 2002, after the huge corporate collapses in Enron. The act pushed for reforms in the auditing procedures and new requirements were put in for internal control as well as addressed employee whistleblowers.[25] After the financial crisis that hit USA in 2008-2009, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 was enacted, it restructured the regulations that were in place earlier and it also extended federal regulation of corporate governance for all public companies. On top of this, a company must comply with the listing rules of the stock exchange it wishes to get listed on- all the major stock exchanges have their own set of rules which have been overseen by the SEC (Securities and Exchange Commission), which also overlooks corporate governance among other things, at the federal level.

SARBANES-OXLEY ACT, 2002

As mentioned above, the Sarbanes-Oxley Act (abbreviated to SOX Act), was legislated in 2002 as a response to the Enron Scandal. It is seen as a progressive legislation which increases the role of the Federal Government in overviewing corporate governance. The highlights of the Act are:

- Creation of the Public Accounting Oversight Board, this would oversee the accounting industry and report to the SEC. This board

[24] Companies Amendment Bill, 2009. https://www.mca.gov.in/Ministry/actsbills/pdf/Companies_Bill_2009_24Aug2009.pdf <Accessed 10 May 2020>

[25] Ruth V. Aguilera and Gregory Jackson (2010) 'Comparative and International Corporate Governance', *The Academy of Management Annals*, 4: 1, 485 — 556, First published on: 05 July 2010 (First)

requires all auditors of public companies and accounting firms to get registered.[26]

- It requires that the CFO and CEO should certify the financial conditions to be reflective of the actual precise financial conditions, results of operations and cash flows if the company in their yearly and quarterly reports. They should also disclose if any changes in the internal control have been made.[27]
- The Act also provides for a whistleblower policy since it recognizes that employees and insiders can help report scandals early on. It provides protection for those employees who have reported frauds and testify in court against their employers.[28]
- The act has also put a ban on executive officers and directors from taking personal loans as well as increased criminal penalties for any violation

Ever since the Act came into place, investor confidence has improved and not only has the regulatory landscape in the US market changed but it has also affected other countries in the world by helping them model their corporate governance codes.

THE DODD – FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT

On June 25th 2010, a House of Senate conference committee reached final agreement on this act and was signed into federal law by President Barack Obama. The act is comprehensive in scope, providing for significant changes to the structure of federal financial regulation and new substantive requirements that apply to a broad range of market participants, including public companies that are not financial institutions.[29] The act provides for corporate governance reforms including, Disclosures regarding chairman and CEO, prohibit broker discretionary voting, no majority voting for director elections and smaller public companies exempted from Sarbanes Oxley internal control requirements. The act for provides for executive compensation reforms including having fully independent compensation committee, pay for performance and pay parity disclosures, hedge disclosures, prohibiting access institution compensations to executive officers, employees, directors of principal holders with compensation that is excessive or that could lead to material financial loss to the financial institution. The act also provided protection to whistle-blowers and extended the scope of liabilities for a doors and abettors of security violations by allowing government in force meant actions against them.

The main purpose of introducing the Dodd Frank Act was to prevent the economy from what it had experienced in 2008 financial crisis and protect the consumers from all the proponents that contributed towards the crisis. It is however observed and argued that this act and the regulatory compliance requirements puts high burden on smaller financial institutions and community banks that have not played any role in the financial crisis. Siding with the critics, the U.S. Congress passed bill in 2018 called the

[26] Section 101 of Sarbanes-Oxley Act, 2002
[27] Section 302 of Sarbanes-Oxley Act, 2002
[28] Sections 806 and 1107 of Sarbanes-Oxley Act, 2002
[29] David S. Huntington, 'Summary of Dodd- Frank Financial Regulation Legislation', July 7 2010, https://corpgov.law.harvard.edu/2010/07/07/summary-of-dodd-frank-financial-regulation-legislation/ <Accessed 13 May 2020>

Economic Growth, Regulatory Relief, and Consumer Protection Act, which rollback significant portion of the Dodd Frank Act.[30] It was signed in to know by president trump on May 24 2008.

COMPARATIVE ANALYSIS BETWEEN USA AND INDIA

INDEPENDENCE OF AUDITORS

It can be noticed that independence of auditors ranks high in importance for both India and USA. It is pertinent to observe that the biggest scandals in both the countries, namely Enron and Satyam, have occurred due to lack of independence of auditors. Auditors act as watchdogs and are needed for an external independent point of view. Both India and USA have explicit requirements regarding the role and independence of auditors.

In USA, the Sarbanes-Oxley Act provides for the Public Companies Accounting Oversight Board to oversee all audit requirements. It is interesting to note that the Naresh Chandra Committee had contemplated on having a similar board in India but the powers that the board has is already distributed among various regulatory agencies such as the SEBI, RBI and the Ministry.

In India, auditors are governed by ICAI Regulations and under certain sections in the Companies Act, 2013. Audit Committees are compulsory for listed companies and there is an express bar on auditors from rendering certain services to their clients such as accounting and book keeping services, internal audit, actuarial services, management services etc.[31] Further, the Companies Act, 2013 has also mandated rotation of auditors for a certain class of companies.

In USA, the PCAOB maintains and enforce regulations and manages the auditing boards but the SEC is the main enforcer for auditor independence. There is no such specific body made in India, but duties on the current ones have been extended. Further the Sarbanes-Oxley Act has also included a gambit of prohibitions, similar to the ones in India's Companies Act.

Hence we can say that independence of auditors is considered as an important requirement in both USA and India as the legal structure is very similar.

INSIDER TRADING

Both India and USA have some form of regulations regarding insider trading but the scope differs. The laws of USA have a stricter and wider reach regarding insider trading. USA uses both the classical/disclose theory and the misappropriation theory by requiring insider to disclose the UPSI to the public and abstain from making trades based on this information and at the same time, the US Sanctions Act, 1984 provides for a fine three times that of the loss avoided or profit gained by the use of the UPSI. SEC also oversees the prevention of insider trading.

On the other hand, India deals with insider trading only under Section 195 of the Companies Act, 2013 and the SEBI (Prohibition of Insider Trading) Regulations, 2015. The term insider trading has not been defined specifically but is understood by reading Regulation 3 (of the Insider Trading Regulations) with Section 12A of the SEBI

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[30] Congressional Research Service, "Economic Growth, Regulatory and Consumer Protection Act https://fas.org/sgp/crs/misc/R45073.pdf Page 2, <Accessed 13 May 2020>

[31] Section 144, Companies Act, 2013.

Act. Regarding the use of misappropriation theory which the US uses, India has gone beyond and included any person with UPSI whereas the US law sticks to just misappropriation of the information.[32] However, the criminal liability requirements in USA are multiple which is not the case for India.
So, keeping these pints in mind, it can be seen that USA has more developed insider trading regulations than India.

INDEPENDENCE OF DIRECTORS ON THE BOARD

Independence of directors is important in both USA and India. Requirements about independent directors is mentioned in the Listing Requirements of Stock Exchanges in USA and in the Companies Act, 2013 and SEBI Regulations in India. Both the countries have similar stances on the need for independent directors.

In India, 1/3rd of the total strength of board of directors is mandated to consist of independent directors (if a company has paid up capital above 3 crore) and if a company is unlisted then there should be at least 2 independent directors, but if the chairman of the company holds an executive position, then at least half the board should consist of independent directors. Clause 49 sets out specific duties regarding directors and if violated, would cause the company to be delisted from the stock exchanges and could have financial penalties imposed on them.

Whereas in USA has larger boards than India and more independent directors.[33] Thought he Sarbanes-Oxley Act does not directly mandate for independent directors, it requires that each member of a public company's audit committee shall be an independent director. Further, NYSE and NASDAQ requires majority of the board of directors to be independent in listed companies and for them to follow the provisions mentioned in the Sarbanes-Oxley Act.

The importance of independent directors can hence be seen in both India and USA.

DISCLOSURE REQUIREMENTS

Disclosure requirements play an important role in both India and USA. In India, disclosures are mandated through the Companies Act, 2013 and SEBI Regulations. These have been incorporated after the recommendations given by the various committees. Disclosure requirements include significant related party transactions, i.e., transaction of the company of material nature, with its promoters, the directors, or the management, or their subsidiaries or relatives, that may have potential conflict with the interests of company at large. Further statutory reporting includes balance sheet and profit and loss account, the boards'/director's reports and auditor's reports. Further in the annual report, the corporate governance section, as mandated by the 2015 SEBI Regulations should include information about board of directors, nomination and remuneration committee,

[32] Arun Kumar Singh & Anil Kumar, Insider Trading: Comparative Analysis of India and USA, *SSRN Electronic Journal* (2014). https://ssrn.com/abstract=2552418 or http://dx.doi.org/10.2139/ssrn.2552418

[33] Shweta Mehrotra, "Corporate Board Structure in the United States and India: A Comparative View", *Indian Journal of Corporate Governance* (December 2015) 10.1177/0974686215602388

remuneration of directors, stakeholders' grievance committee, general body meetings, Means of communication, and general shareholder information.

Meanwhile in the US, similar disclosure requirements exist which come within the ambit of the Sarbanes-Oxley Act, SEC Regulations and the Dodd-Frank Wall Street Reforms. Mandatory disclosures include disclosure regarding executive compensation. The SEC requires two annual reports to be filed by public listed companies, one for the SEC and the other for the shareholders of the company. The annual reports to the shareholders must contain the certified financial statement which should include a two year audited balance sheet and a three year audited cash flow and income statement. Apart from these the annual reports should also have the management's discussions about the firm's financial liquidity and other such comprehensive details. Further, directors and officers of the corporation should be identified as well as disclose the qualification standards of the directors and their compensation.

Hence we see that disclosure requirements are quite extensive for both USA and India, with both countries requiring disclosures on common subjects.

PRESENCE OF WOMEN IN THE BOARD

While getting women on boards as a measure of fairness, equality of opportunity and social justice, such inclusion must be justified to insure better corporate performance. The reasons will include increasing diversity of opinions in the boardroom and providing Female role models, influence on decision making and leadership styles of the organization, ensuring better boardroom behaviour, woman directors tend to be younger than their male colleague on the board , so it may benefit to the bored with new ideas and strategies, having women in key positions is argued to be associated with long term success and competitive advantages as well as women on boards or adding value to long term success of company to come women's distinctive set of skills.[34] While in USA there is no law mandating the states to have women on board, India has included the in its new Companies Act, 2013, that prescribed companies shall have a woman director. In USA, in 2019, California became the first state to pass a bill, that publicly traded companies shall have at least one female director. Female representative on Fortune 500 boards has been inching up in the United States with women now holding about 20 percent of Fortune 500 board seats.[35] Data given by Deloitte shows that in USA board seats held by women are 14.2% while in India it is 12.4%.[36] Research has further shown that both India and USA has been extremely slow in the progress of increasing diversity.

BOARD LEADERSHIP STRUCTURE

In United States, Since 2010, Public companies have been required to disclose their board leadership structure, specifically

[34] Simmi Arora, Naresh Kumar, "Woman on Boards, A gap analysis of India vis a vis the world", *Chartered Secretary* (March 2016)

[35] "Women in Boardroom- A global perspective" (5th Edition) https://www2.deloitte.com/content/dam/Deloitte/za/Documents/technology-media-telecommunications/za_Wome_in_the_boardroom_a_global_perspective_fifth_edition.pdf <Accessed 17 May 2020>

[36] *Ibid.*

whether the same person served as CEO and chair of the board(known as CEO duality or combined board leadership structure) or whether two individuals are in those positions, and why they believe their leadership structure is appropriate given their specific characteristics or circumstances.[37] On the other hand in India neither the companies act nor clause 49 directly say anything about the board structure. Generally, companies disclose their structure in corporate governance reports which is part of the annual report but there is no such mandate. More and more companies in both the nation are thinking of combining the two roles, based on the fact that this might eliminate some confusion. However, both the countries do not hole much importance to the board leadership structure.

WHISTLE BLOWING POLICY

Whistle blowing relates to the action taken by a person against the company indulging in illegal unlawful activities. There can be various types of whistle blowing, including internal, external, individual and institutional. Usually the motive behind this is to highlight possible risk, to enforce ethical conduct, to protect public interest and to inspire other employees. In India from 2003 and three Various bills have been passed so as to address the issue of whistle blowing. These bills include public interest disclosure and protection of persons making disclosures bill, 2010, the Whistle Blowers protection bill, 2011. These bills Include provisions protecting the whistle blowers from any lash out by the Corporation against them. These bills and laws also include protection of the Corporation from false information furnished by the whistle blower in order to destroy the refutation and the dignity of the company.

In USA as well after the case of Sherron Watkins, many legal provisions regarding the whistle blowers were introduced. These provisions include False Claims Reform Act, 1986, Sarbanes- Oxley Act of 2002, Fraud Enforcement and Recovery Act, 2010 and Consumer Products and Safety Improvement Act, 2008. Sarbanes- Oxley Act of 2002 provided Whistle blowers and give them the right to a jury trial in certain cases. There are tremendous amount of laws in USA as compared to India. In India whistle blowing was quite narrow. The reason behind specific laws in United States is due to continuous media exposing of the government frauds and company frauds that lets to the demand of initiating these laws. There are many loopholes in Indian laws such as the non-protection of family members etc. so it is highly recommended that Indian government should make laws which give them overall protection

CONCLUSION

The study of the overall comparison of Corporate Governance Codes of US and India reveals that most of the practices of the Corporate Governance are common. The difference is the approach of the regulators and support of the stakeholders in implementing the same. The role of monitoring agencies such as SEC and SEBI would be very crucial in coming days. It is evident that both India and USA have gone through some similar scandals and based on which they have follows a similar trajectory of developing its corporate governance

[37] Shweta Mehrotra, "Corporate Board Structure in the United States and India: A Comparative View", *Indian Journal of Corporate Governance* (December 2015) 10.1177/0974686215602388

environment. However, nuanced differences still crop up within the systems when compared. The reason behind this, based on the research can be concluded to be that the differences between the corporate governance models in India and the US can be said to be due to differences between the business environment and cultures.

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