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A Comparative Study of Corporate Governance in India and the USA

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Abstract:
This paper explores the concept of corporate governance with the comparison in governance framework, board structure and its role, Shareholder Rights and Activism, Enforcement and Compliance, Remuneration to Board Members, Executive Compensation, Terms of service of Directors, Composition of the Board of Directors in corporate governance of two major countries USA and India. The study reveals that most of the practices of the Corporate Governance are common but also there is dissimilarities in terms of board size, board composition and independence, leadership structure, and gender diversity in both India and Unites States. The study indicates that US Companies have larger board with majority of independent directors prominence of combined leadership structure, relatively more gender diverse as compared to India. The U.S. system benefits from a well-established regulatory framework with strong enforcement and active shareholder engagement. In contrast, India's governance framework is evolving with recent reforms aimed at improving practices, but challenges such as family-run businesses and inconsistent enforcement remain.

Keywords: Corporate Governance, board structure, regulatory framework, shareholders' activism.

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Introduction

Corporate Governance is a critical framework of rules and practices that guides an effective management of corporations, making sure there is fairness and accountability in company's relationship while incorporating with the interests of stakeholders. In a globalized economy, effective corporate governance has become essential not only for the sustainability and growth of companies but also for maintaining investor confidence and protecting stakeholder interests. This research paper dives into the intricacies of corporate governance in two different countries, India and the USA, two major economies with distinct regulatory environments and business practices.

This study highlights the large role of regulatory bodies and international governance standards in creating the governance landscape. Additionally, it investigates the diverse governance models adopted in both United States of America and India, emphasizing on the many factors that influences the framework of the governance.

In the USA, after bankruptcies of prominent companies such as US energy giant Enron, telecommunication giant Worldcom, Parmalat and multinational newspaper group

Hollinger, the issue of corporate governance has received global attention.

corporate governance has been shaped by extensive legal and regulatory frameworks designed to ensure transparency and accountability. Landmark legislations such as the Sarbanes-Oxley Act (2002) and the Dodd-Frank Act (2010) have established stringent requirements for financial disclosures, internal controls, and executive compensation, aiming to enhance investor protection and prevent corporate fraud. These regulations are complemented by a robust market-driven approach, where independent directors and active shareholder engagement play critical roles in governance practices. The U.S. system is often cited as a model for effective corporate governance due to its comprehensive regulatory environment and active enforcement mechanisms. Data from the year 2023 shows that around 70% of the companies in the U.S. have majority independence boards, which indicates a high influence by shareholders.

In contrast, The Satyam scam of 2009 and reebok scam of 2012 shattered the myth of good corporate governance in India. India's corporate governance landscape has undergone significant reforms, particularly with the enactment of the Companies Act (2013) and the strengthening of guidelines by the Securities and Exchange Board of India (SEBI). These reforms emphasize the role of independent directors, audit committees, and enhanced corporate transparency. However, challenges such as the influence of family-run businesses, inconsistent enforcement, and cultural factors continue to affect the effectiveness of governance practices. Corporate governance in India is more heavily concentrated in ownership, where families and promoters lead from the front. According to a 2022 study by Securities and Exchange Board of India, about 50% of Indian companies are family owned, thereby reducing the idea of exercising the power of any decision making by minority shareholders.

Thus, This study examines these issues to understand how governance frameworks in both countries address corporate accountability and stakeholder protection, providing a comparative analysis that highlights best practices and areas for improvement.

Review of Literature

Shleifer and Vishny (1997) argue that corporate governance mechanisms are vital for aligning managerial actions with shareholder interests, thereby minimizing agency costs. Their theory emphasizes the importance of board structure, executive compensation, and shareholder rights in promoting effective governance.

Debasis Pahi and Inder Sekhar Yadav (2019) suggests in their study that the stronger corporate governance having companies are paying higher dividends and there is positive correlation between corporate governance and dividend payment by the firms.

Samridhi Suman and Shveta Singh (2020) Through their study they found that Research and development investments are substantially influenced by the presence of corporate governance.

The USA has one of the most developed corporate governance frameworks, shaped by landmark legislation such as the Sarbanes-Oxley Act (2002) and the Dodd-Frank Act (2010). Coffee (2007) discusses how these laws introduced stringent requirements for financial reporting, internal controls, and executive compensation, aiming to enhance transparency and prevent corporate fraud.

Roe (2003) highlights the role of independent directors and the separation of the CEO and Chairman roles, which are pivotal in maintaining robust governance standards in U.S. corporations.

Khanna and Palepu (2000) examine the impact of these reforms on governance practices, emphasizing the increased focus on independent directors and audit committees.

Nair and Bansal (2015) identify persistent challenges, such as the influence of family-run businesses and inconsistent enforcement of regulations, which affect the effectiveness of governance practices in India.

Ankur Shukla, et al., (2020) Their study conclude that the market risk of Indian banks is increasing due to presence of Independent directors in board panel.

A. Shivani (2022) analyzes the events that have hampered the development of corporate governance in India and subsequently conducts a global comparative study of leadership.

Mehrotra (2018) demonstrates in their study that there is still a requirement of developing more appropriate solutions that would contribute in the policy formulation in order to make corporate governance standards more effective for the indian conditions.

Bhanotu(2020) reviewed that corporate governance is impacted by the concentration in ownership structure and complying with existing rules and regulations on listed companies' practices.

Objective of the Study

1. To compare and contrast the corporate governance frameworks and practices in India and the USA.
2. To assess the impact of regulatory frameworks on corporate governance effectiveness in both countries.
3. To identify best practices and areas for improvement in corporate governance within each country.

Gap analysis of the study

On the basis of evaluation of literature and objectives, researcher found the gap in this area. After considering a few research have been taken for the study, researcher is found following gap:

- **Regulatory Framework Comparison:** The study may not deeply explore the distinct regulatory frameworks of India and the USA, missing out on detailed comparisons of key laws like the Sarbanes-Oxley Act and the Companies Act.
- **Cultural and Market Differences:** It might overlook how cultural attitudes and market dynamics uniquely influence corporate governance in each country, particularly between family-owned and publicly traded companies.
- **Effectiveness and Outcomes:** The study could lack a thorough assessment of the actual effectiveness and outcomes of corporate governance practices, such as their impact on business performance and economic stability.

Scope of the Study

This study provides a comparative analysis of corporate governance practices in India and the USA. It covers:

- ✓ Regulatory frameworks and legal requirements governing corporate governance.
- ✓ Board structures, roles, and the composition of boards in both countries.
- ✓ Shareholder rights, activism, and participation mechanisms.
- ✓ Enforcement and compliance issues and their impact on corporate governance.

Research Methodology

The research adopts a comparative case study approach, analysing the corporate governance frameworks and practices in India and the USA. This approach involves a detailed examination of regulatory documents, academic literature, and case studies of notable corporate governance issues.

Data Collection

Data for the study is collected from:

1. **Regulatory Documents**: Analysis of the Sarbanes-Oxley Act, Dodd-Frank Act, Companies Act 2013, and SEBI guidelines to understand the legal frameworks governing corporate governance.
2. **Academic Literature**: Review of scholarly articles, books, and papers on corporate governance practices and theories.
3. **Case Studies**: Examination of significant corporate governance failures and reforms, such as the Enron scandal (USA) and the Satyam scandal (India), to assess practical implications and lessons learned.

Data Analysis

The data is analysed through a comparative lens to identify key similarities and differences in governance practices. The analysis focuses on evaluating the effectiveness of governance mechanisms, regulatory enforcement, and shareholder participation in both countries. Recommendations for improvements are based on the findings from the comparative analysis.

Data Analysis & Interpretation

Governance Frameworks

The U.S. corporate governance framework is characterized by its strong legal protections for shareholders and rigorous regulatory requirements. The Sarbanes-Oxley Act mandates stringent internal controls and financial disclosures to enhance transparency and accountability. The Dodd-Frank Act introduces reforms related to executive compensation and shareholder rights. These regulations collectively contribute to a robust governance framework that emphasizes investor protection and corporate accountability.

India’s governance framework has been strengthened by the Companies Act 2013 and SEBI regulations. It focuses on protection of minority shareholders, accountability of the board of directors and management of the company; timely reporting and adequate disclosures to shareholders. These reforms also emphasize the role of independent directors, audit committees, and corporate transparency. However, challenges remain, such as the influence of family-run businesses and inconsistent enforcement of regulations, which impact the effectiveness of governance practices.

In 2022, over 400 class-action suits related to corporate governance matters were filed in the U.S., which contributed towards strengthening the country's legal framework. In India, while the legal protections do exist, enforcement tends to be weaker which makes it harder for minority shareholders to seek redress. Cases related to corporate governance in India were at a much lower level, less than 50 cases as reported in the year 2022. This concludes a difference of almost 350 cases between both countries in 2022.

Board Structure and Roles

In the U.S. system of corporate governance, a great deal of emphasis is placed on board independence. U.S. boards typically consist of a majority of independent directors and have separate roles for the CEO and Chairman. This structure is intended to enhance oversight, reduce conflicts of interest, and ensure that the board provides effective governance. Independent directors play a crucial role in monitoring management and ensuring that shareholder interests are prioritized.

Indian boards also include independent directors and committees, but often face challenges related to the dual roles of CEO and Chairman. The presence of family members in senior management positions can impact governance practices by potentially reducing the effectiveness of oversight and decision-making.

Under the Sarbanes-Oxley Act, it is required that a majority of board directors should be independent. In 2023, the average U.S. board had 85% of its directors as independent board members; however in India, the rules have some degree of board independence, but actual practice is much more relaxed. SEBI's rules provide for the minimum one-third of the board to be independent members, nevertheless actual implementation of this varies widely and the actual figure of listed companies meeting this criterion reaches about 60%.

Shareholder Rights and Activism

In the United States, it is nearly shareholder-driven corporate governance. Powers in influencing the decisions of the company through their voting rights and shareholder meetings are enjoyed by the shareholders in the United States. Shareholders in the USA have extensive rights, including the ability to propose resolutions, vote on significant issues, and engage in activism to influence corporate policies. Shareholder activism is a prominent feature of the U.S. governance landscape, with investors actively participating in corporate decision-making and policy changes.[8]

While shareholder rights are protected by law in India, activism is relatively underdeveloped compared to the USA. Recent reforms aim to enhance shareholder engagement, but practical challenges, such as limited investor participation and weak enforcement, affect the extent of shareholder influence.

Data from the year 2023 shows that around 70% of companies in the U.S. have majority-independent boards, which indicates a high influence by shareholders. In contrast, corporate governance in India is more heavily concentrated in ownership, where families and promoters lead from the front. According to a 2022 study by the Securities and Exchange Board of India, about 50% of Indian companies are family-owned, thereby reducing the idea of exercising the power of any decision-making by minority shareholders.

Enforcement and Compliance

The U.S. regulatory environment is characterized by stringent enforcement mechanisms. Regulatory bodies such as the Securities and Exchange Commission (SEC) oversee compliance and take action against violations. This strong enforcement framework contributes to high levels of corporate accountability and investor protection. CSR is largely voluntary in the U.S., and it is driven by market forces as well as shareholder expectations.

Enforcement in India can be inconsistent, with challenges in monitoring and implementing regulations. Recent efforts to strengthen regulatory oversight and increase penalties for violations have been made, but issues related to enforcement and compliance persist.

The SEC imposed fines of $4.2 billion for corporate governance failure in the year 2022 alone. In India, while SEBI has been doing its bit to strengthen the norms on governance, the enforcement has been patchy. SEBI imposed penalties of USD 250 million in the year 2022, and most companies still find some way or another to avoid very rigid compliance.

Remuneration to Board Members

In the United States, the board of directors typically determines the compensation for directors, often based on recommendations from a compensation or nominating committee. The board may also consult with independent compensation consultants. The US Security Exchange Commission announced that most public companies should disclose the remuneration paid to the personnel as per the Dodd-Frank Act of Section 953 (b), which had issued on 18th September 2013.

As per Regulation 19 of SEBI (LODR) Regulations, 2015 the remuneration Committee should comprise 3 members and they must be non-executive members, and two-third of them should be Independent board members. The Chairperson of Remuneration Committee should be Independent board members. They should conduct a meeting at least once in a year.

In the US, board members receive about $112,575 as of 2024, with the average salary range falling between $86,782 and $139,025. On average, the compensation for board members can be much higher, particularly those in large publicly traded companies. As of September 2024, the average salary for a board member in India is Rs. 72,500, according to Glassdoor, job search and career community. The average annual pay for independent directors in India is Rs. 37.5 lakhs, with a range of Rs.3.5 lakhs to Rs. 96 lakhs.

Executive Compensation

Executive pay in America is mainly performance-related, with a large percentage composed of stock options and bonuses. This is to be disclosed as a norm of corporate governance. Corporate are struggling to explain the basis of compensation offered to the executives of the company.

The rules in India also set much firmer limits on executive pay to prevent excessive risk-taking and link interest more closely to long-term company performance. while the U.S. has fewer limits.

For example, the average compensation of U.S. CEOs in 2022 was around $18 million, with the majority in the form of stock options. In India, this pay is greatly different with the average CEO bringing home around $1.2 million in 2022. **Terms of service and gender diversity of Directors:**

It is suggested that both countries' companies board rooms should be more gender diverse as board with different behaviour, attitudes and orientation. Boards of US listed companies are relatively larger with majority of independent directors on board, prominence of combined board leadership structure and relatively more gender diverse as compared to Indian boards. In the US, there are no specific provisions defining the term of a director to serve on the company, neither mandatory nor recommendatory. skills set will contribute more new insights and fresh perspectives in the board.

Gender Diversity in board of Indian listed companies is very minimal in India. With context to Terms of service it is recommended that the non-executive directors should serve as independent directors in any company not more than nine years.

Committees to be formed under corporate governance

US corporate Governance Code requires that listed companies must form three committees: Audit Committee, Governance/Nominating Committee, Compensation Committee.

Whereas, In India, Corporate Governance Code under Clause #9 requires to form committees of the board: Audit Committee, Shareholder's / Investor's Grievance Committee, Remuneration Committee.

Composition of the Board of Directors

In US, neither SEC nor any federal legislation has rules on board size and therefore number of directors varies significantly from company to company. However, individual stock exchanges such as NYSE have determined that listed companies must have majority of independent directors.

In India, Clause 49 determines the Board composition based on the Chairperson of the Board. If Chairperson is an executive Director, more than 50% directors on the Board should be Independent Directors If Chairperson is a non-executive Director, more than 33%

directors on the Board should be Independent Directors.

Limitation of the study

The following limitations are:

1. The study may not thoroughly analyse the different regulatory frameworks of corporate governance in India and the USA.
2. It might not fully consider how cultural and market differences influence corporate governance practices in each country.
3. The study could lack an evaluation of the effectiveness and impact of these governance practices on business performance and economic stability.

Conclusion

The comparative study of corporate governance practices in India and the US reveals both strengths and areas for improvement in each country. The U.S. system benefits from a well-established regulatory framework with strong enforcement and active shareholder engagement. In contrast, India's governance framework is evolving with recent reforms aimed at improving practices, but challenges such as family-run businesses and inconsistent enforcement remain.

Overall comparison of Corporate Governance codes of US and India reveals that most of the practices of the Corporate Governance are common but also there is dissimilarities in terms of board size, board composition and independence, leadership structure, and gender diversity in both India and Unites States. The study indicates that US Companies have larger board with majority of independent directors prominence of combined leadership structure, relatively more gender diverse as compared to India.

Recommendations for improving corporate governance in India include strengthening enforcement mechanisms, enhancing shareholder participation, and ensuring greater separation of executive roles. Selection procedure for independent directors should be changed. there should be emphasis on quality of the meeting rather than quantity of the meeting in Indian listed companies. The U.S. could focus on adapting governance practices to address emerging global trends and challenges, ensuring continued relevance and effectiveness. In US, Separate Board leadership structure is required as separate role of CEO and Chairman brings more clarity in performing their duties which can leads to better performance. Lastly, It can be said that the role of monitoring agencies such as SEC and SEBI would be very crucial in future.

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