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PROBLEMS OF CORPORATE GOVERNANCE IN USA

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ABSTRACT: *The United States of America is the biggest economy of the world producing twenty one percent of total world output through millions of business firms operating in its territory. It is generally assumed that US human capital is more productive and business firms are more efficient. The US firms have been obtaining efficiency gain vis-à-vis their European and Asian competitive firms. This is claimed to be due to good corporate governance. The objective of this study is to study the level of corporate governance because in spite of being efficient economy there are a large number of corporate failures and corrupt practices. The authors have intended to investigate the causes of corporate governance problems in the United States and their possible solutions. The author used secondary data taken from different relevant Books, Journals and US Bureau of Economic Analysis. The nature of the research is qualitative and as such the author used qualitative tools to study the level of corporate governance. The author founds that US business firms have also been facing agency problem, corrupt practices like inside trading in the capital market and misusing resources despite the fact that the United States have strongly regulatory framework. But this regulatory framework is rigid, having many loopholes, providing opportunity to self-interest-seeking managers to manipulate them. The authors suggest that existing regulatory framework needs to be re-examined to make it flexible, keeping in view rapidly changing corporate environment.*

KEYWORDS: Corporate Mis-governance, Agency problem, Moral Hazards

INTRODUCTION

Corporate governance is dealing with "problems that result from the separation of ownership and control." From this perspective, corporate governance would focus on: the internal structure and rules of the board of directors; the creation of independent audit committees; rules for disclosure of information to shareholders and creditors; and, control of management. A recent academic survey began with the quote: "Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment. Modern corporate governance started in 1992 with the Cadbury Report. Cadbury was the result of numerous high profile company collapses and is concerned mainly with protecting weak and dispersed shareholders against self-interested directors and managers. Corporate Governance is a step towards strengthening of the organization to face the challenges. Corporate Governance is to takeover the role of the shareholders, stakeholders, vendors, suppliers & employees by the top Managers and CEO of the company. This would

involve that as stakeholders, vendors, suppliers & employees have invested their money, material, effort and faith in the company. Top managers and CEO should give importance to these business pillars. Corporate Governance is a process and device by which the capital market monitors the actions of corporate management, which means that the company is required to act in accordance with the listing agreement of Stock Exchanges and other monitoring agency.

Corporate Governance has been defined in different ways by different writers and organizations. Some define it in a narrow perspective to include in it only the shareholders, while other want it to address the concerns of all stakeholders. Some talk about corporate governance being an important instrument for a country to achieve sustainable economic development, while some others consider it as a corporate strategy to achieve a healthy image for a long tenure. To people in developing societies and intermediary economies, it is a necessary incentive to direct in more powerful and exciting institutes of control. To other people it provides another dimension to corporate ethics and social responsibility of business. Thus corporate governance has different meaning to different people. But to all, corporate governance is means to an end and that end is being long term shareholders, and more outstandingly stakeholder's value. Thus, all authorities on the subject are one in recognizing the need for good corporate governance practices to achieve the end for which corporate are formed. They identify some governance issues being vital and critical to achieve these objectives. These are following:

Distinguishing the roles of Board and Management:

Many companies emphasize that the business is to be managed by the direction of the board. In such practices, the responsibility for managing the business is delegated by the board to the CEO, who in turn delegates the responsibility to other senior executives. Thus, the board occupies a key position between the shareholders and the company's management. As per this arrangement, the board of a listed company should perform their functions as following;

a) Select, decide the remuneration and evaluate on a regular basis, and when necessary, change the CEO.
b) Oversee the conduct of the company's business to evaluate whether or not it is being correctly managed.
c) Review and, where necessary, approve the company's financial objectives and major corporate plans and objectives
d) Render advice and counsel top management including the board of directions.
e) Identify and recommend candidates to shareholders for electing them to the board of directors.
f) Review the capability of systems to comply with all applicable laws and regulations.
g) All other functions required by law to be performed

Composition of the board:

A board of directors is a "committee elected by the shareholder of a limited company to be responsible for the policy of the company. For full time functional directors are appointed there being responsible for some particular work. The composition of board of directors refers to the number directors having different kind of experience that participate the work of the board. Over a period of time there has been a change as to the number and proportion of different types of directors in the board of limited company. The board of directors of a company shall have an optimum combination of executive and non-executive directors with not less than fifty

percent of the board of directors to be non-executive directors. The number of independent directors would depend whether the chairman is executive or non-executive. In case of a no executive chairman, at least one third of the board should comprise independent directors and in case of executive chairman, at least half of the board should be independent directors.

Separation of the roles of the CEO and chairperson:

The composition of the board is a major issue in corporate governance as the board acts as a link between the shareholders and the management and its decisions affect the performance of the company. Professionalization of family companies should commence with the composition of the board. All committees that studied governance practices all over the world, starting with the Cadbury Committee, have suggested various improvements in the composition of boards of companies.

It is now increasingly being realized that the practice of combining the role of the chairperson with that of the CEO leads to conflicts in decision making and too much concentration of power in one person resulting in unhealthy consequences. Combining the role of both the CEO and chairperson removes the check on senior management's activities. In large corporations, the job of the CEO as well as that of the chairman may be heavy and one person may not be able to deliver what his expected to, competently, efficiently and objectively. That is the reason on corporate governance recommends strongly that the chairman of the board should be an independent director in order to provide counterbalance and check to the power of CEO.

Should The Board Have Committees?

Many committees on corporate governance have recommended in one voice the appointment of special committees for Nominations, Remuneration and Auditing.These committees would reduce the burden of the board and enhance the effectiveness. These committees should have written outlining their authority, duties and clear procedures for reporting back to the board. When these committees are peopled with independent directors selected for their competence, professional expertise in these chosen fields and long years of work experience would help the respective committees decide issues objectively and in a manner that would promoted the long term interests of the organization.

Appointments and Re- Elections of Directors:

Shareholders elect directors to the board. Shareholders are a legion, crowd and throng in large companies also scattered. In most cases, the board selects and appoints the prospective director and gets the person formally elected by the shareholders at the Annual General Body Meeting. Shareholders in fact only endorse the board's nominees and it is only in rest of rare case that shareholders refuse to confirm the board's nominees for directorship. There are other issues of corporate governance in relation to the board's appointment such as appointment of a nomination committee, terms of office, duties, and remuneration and reelection of directors and composition of the board on which several committees have made their own recommendations. Corporate governance tends to focus on a simple model like Shareholders elect directors who represent them. Directors vote on key matters and adopt the majority decision. Decisions are made in a transparent manner so that shareholders and others can hold directors accountable. The company adopts accounting standards to generate the information necessary for directors, investors and other stakeholders to make decisions. The company's policies and practices adhere to applicable national, state and local laws. Focusing on these

types of internal control processes, it is quite natural when the subject is corporate governance within the advanced market economies.

The essential fundamentals for which Corporate Governance has started are as following:

- **Transparency** : A company is required to transact their business in a manner which is highly transparent and their books of accounts should reflect the same
- **Accountability**: Corporate Governance ensures the accountability of Board of Directors or senior management to the various stake holders within and outside the company
- **Control** : To protect the interest of the shareholders the Apex monitoring body for example Security and Exchange Commission exercise control over the management of company through various compliances
- **Trusteeship** : Board of directors must act as the trustees of the stakeholders and good Corporate Governance ensures the same
- **Ethics**: Good ethical practices are the foundation of any successful corporate governance and ensures fairness in all its activities

Directors' and Executives' Remuneration

This is one of the mixed and vexed issues of corporate governance that came to the centre stage during the massive corporate failures in the US between 2000 and 2002. Executive compensation has also in recent time become the most visible and politically sensitive issue relating to corporate governance. According to the Cadbury Report: the over riding principle in respect of Board remuneration is that shareholders are entitled to a full and clear statement of directors' present and future benefits, and how they have been determined. Other committees on corporate governance have also laid emphasis on other related issues such as pay of performance, severance payments, and pension for non executive directors and appointment of remuneration committee and so on. However while controversy often surrounds the size or quantum of remunerations, this is not necessarily an issue of corporate governance. The key corporate governance issues are; Transparency in executive compensation, Pay for performance whether the payment is justified, Process for determination, Severance payments of pay and Pensions for non executive directors

Disclosure and Audit:

The Cadbury Report termed the annual audit as one of the cornerstones of corporate governance. Audit also provides a basis for reassurance for everyone who has a financial stake in the company. Cadbury Report stressed that the board of directors has a bounded responsibility to present the shareholders a clear and balanced assessment of the company's financial position through audited financial statements. There several issues and questions relating to auditing which have an impact on corporate governance as following:

1) Should boards establish an audit committee?
2) If yes, how should it compose?
3) How to ensure the independence of the auditors?
4) What precautions are to be taken or what are the positions of the state and regulators with regard to provision of non-audit serves rendered by auditors?
5) Should individual directors have access to independent resource?
6) Should boards formalize performance standards?

These questions are being answered with different perceptions and with different degrees of emphasis by various committees and organization that have gone into and analyzed these issues in depth

Protection of shareholder rights and their expectations:
This is an important governance issue which has considerable impact on the rights and expectations of shareholders. Corporate practices and polices vary from country to country. These are a number of questions relating to this issue such as;

1) Should companies always adhere to one share one vote principle?
2) Should companies retain voting by a show of hands or by poll?
3) Can shareholders' resolutions be boundless? That is to place together before shareholders for approval a resolution that contains more than one discrete issue
4) Should shareholder approval be required for all major transactions?

These questions have drawn out answers with different emphasis from various committees and organizations that have addressed these issues

Dialogue with institutional shareholders:
The Cadbury Committee recommended that institutional investors should maintain regular and systematic contact with companies, apart from their participation in general meetings of shareholders, use their voting rights positively, take a positive interest in the compositions of the board of directors of companies in which they invest, and above all, recognize these whose money they have invested by influencing the standards of corporate governance and by bringing about changes in companies when necessary, rather than by selling their shares, and quitting the companies. If institutional investors have to exercise their rights and carry out their responsibilities, companies have to provide them the required information and facilities.

The United States is often seen as being the paradigmatic case of the shareholder oriented or market based approach to corporate governance. Ownership of corporations is dispersed, but involves high engagement from institutional investors, such as pension funds and other financial institutions. Corporate boards are small, have a high proportion of outside or independent members, and utilize committees to improve processes of board. The internal and external aspects of corporate governance are linked through the audit firms that certify the flow of information from managers to markets. The market for corporate control exerts a final discipline on poorly performing firms, who face a heightened risk of takeover. These different elements are also thought have strong institutional complementarities, operating as a positive and mutually reinforcing system of effective corporate governance. United States corporate governance system seem to be in terrible shape. The business press has focused relentlessly on the corporate board and governance failures at Enron, WorldCom, Tyco, Adelphia, Global Crossing, and others. Top executive compensation is also routinely criticized as excessive by the press, academics, and even top Federal Reserve officials.

A wave of corporate scandals in the United States early this century Enron, Tyco, WorldCom and the like other led to extraordinary focus by the White House and the US Congress on corporate governance. This concluded in the enactment in July 2002 of the Sarbanes Oxley Act, and has been followed by significant regulation and rule making affecting corporate affairs by the US Securities and Exchange Commission (SEC) as well as by stock market self regulatory bodies for example the New York Stock Exchange (NYSE) and National Association of Securities Dealers Automated Quotations, commonly known as NASDAQ

Stock Market. The full impact of these rules has not yet been felt and a number of significant proposals are still pending.

Sarbanes Oxley has not changed the basic structure of corporate governance in the United States: day to day management of a corporation is still in the hands of the management, subject to oversight by a board of directors elected by shareholders. However, the major aim of the reforms has been to establish clear accountability of a public company's chief executive officer (CEO) and chief financial officer (CFO) for the accuracy of the company's public disclosures, and to strengthen and reinforce the role played by the board of directors and key board committees especially the audit, compensation and governance committees in the oversight of corporate management. The CEO and CFO in a company that is public in the United States must personally certify as to the accuracy of the company's public disclosures, and to its disclosure controls and internal control processes. In addition, the majority of the board of a US company with a US listing, as well as the entire membership of each of those committees, will be required to be independent under new independence standards.

LITERATURE REVIEW

Literature review focuses on the problems and issues of corporate governance including responsibilities of board of directors and managers, responsibilities of stakeholders and principles of corporate governance. This review explores the development of techniques for managing and correction of ethical issues, and examines the problems of corporate governance in United State of America. Corporate governance in the United States has traditionally been a subject of state corporate law, focused on the relative roles and powers of shareholders, the board of directors and corporate officers in relation to corporate action, decision making and oversight of management. A more basic issue remains open, though: Ought government policy to support family run control pyramids or break them up. (Morck et al 2000) argue that entrusting extensive corporate control to a few old families is generally undesirable.

Family Firms:

Control of corporate assets by wealthy families in economies is common, and control pyramids concentrate governance powers in tiny elite in many countries. Many countries entrust the governance of their large corporations to a handful of wealthy families. These families use control pyramids to affect these powers. Such control pyramids make firms exposed to a range of serious governance problems. A concerted effort to improve a country's institutions is needed before diffuse ownership is desirable. Anderson and Reeb (2003) refer to any firm with a dominant shareholder as a family firm. Systematic differences in the governance of an economy's great corporations might affect its macroeconomic performance. New money and old family money vie for importance in Latin America, and the United States. Anderson and Reeb (2003) find evidence consistent with large shareholders in the United States improving firm performance. Empirical work to date is broadly consistent with this viewpoint. Public shareholders are myopic, and focus only on short term earnings, have long been exposed. Corrupt or inefficient courts doubtless magnify the importance of a reputation for fair dealing. A connection with such a family, however distorted by layers of pyramidal control, may be a great asset to a firm operating in a country where legal remedies for fraud are absent. A well-developed legal and regulatory system that makes public investors confident of their property rights encourages families to sell out. Heirs may come to realize that professionals can run the family's firms better, and may opt to become passive investors with diversified portfolios of

stock in firms they do not control. Poor education systems leave potentially brilliant managers to lives as illiterate peasants, and may well leave the members of a few dominant families, able to afford to send their sons to elite educational institutions abroad, the most able managers. While governance problems in widely held firms clearly can be serious, we argue that family control can give rise to other, potentially worse, corporate governance problems. Schultz, Lubatkin, Dino, and Buchholtz (2001) convincingly point out that agency problems can occur between family members. We argue that, in addition to these problems, another set of agency issues arise when family controlled firms organized into business groups obtain outside equity financing. These agency issues are: the use of pyramidal groups to separate ownership from control, the entrenchment of controlling families, and non-arm's-length transactions between related companies that are detrimental to public investors.

Role of the audit committee:

The role of the audit committee, in particular, has been significantly strengthened and expanded at corporate level. All members of the audit committee must be independent under a more stringent Sarbanes Oxley definition of 'independence'. In addition to certain stock exchange financial literacy requirements, the SEC has adopted a disclosure requirement as to whether a financial expert sits on the company's audit committee. There is a clear sense among public company directors that the personality and expertise of the chairman of the audit committee are crucial to the system of corporate governance.

One of the cornerstones of Sarbanes Oxley is a focus on the independence of the company's auditor. Sarbanes Oxley makes it law in the United States that the independent auditor of a US public company ultimately reports to the company's audit committee, not its management. Further, to avoid conflicts of interest on the part of the audit firm, the provision of many categories of non-audit services to the client is now prohibited, while any permitted category of non-audit service must be preapproved by the audit committee. The company is required to break out and disclose the amounts paid to the auditor for audit and non-audit services. To reinforce this independence theme and further avoid well-established relationships with management, the audit partner and other key personnel of that firm engaged with the client must rotate after specific duration.

Shareholder Value:

By the 1990s, the trend toward greater shareholder influence continued, but was reshaped by the responses of managers. On one hand, executives sought to defend their own power by shielding firms from unwanted takeover bids. On the other hand, managers aligned themselves increasingly with the interests of shareholders through new forms of executive pay and adopting the ideology of shareholder value (Dobbin & Zorn, 2005). Shareholder value refers to the concept that the primary goal for a company is to increase the wealth of its shareholders by paying dividends and/or causing the stock price to increase. Somewhat paradoxically, although shareholder power was tamed, shareholder value became a powerful new ideology. In 1992, federal proxy rules were revised to give shareholders enhanced latitude to communicate amongst themselves (Schwab & Thomas, 1998). The scope of issues targeted by shareholder activism expanded further to cover changes in board structure and function, as well as executive and director compensation. The influence of shareholder activism remained exciting, but modest on the whole. Even the most activist investors have limited resources devoted to corporate governance and institutional investors rarely get involved in matters of

company specific policy, make shareholder proposals or seek direct representation by nominating candidates to the board of directors (Black, 1998, Choi & Fisch, 2008).

Despite the growing importance of independence, two facts are worth noting. First, the legal definition of an independent director remained rather weakly developed and was specified only in state corporation law. Second, a majority of U.S. firms still combined the role of CEO and Chairman within the board. This problem puts some doubt on the genuine independence of other board members. A number of boards from this period note that outside directors felt strong loyalty to the CEO regarding issues such as "golden parachutes" (Wade, Charles A. O'Reilly & Chandratat, 1990) and that CEO influence led to boards with demographically similar (Westphal & Zajac, 1995). In particular, the rise of equity based pay such as stock options had given managers a greater stake in promoting restructuring and orientating their strategies toward the stock market. In 1991, the SEC changes rule 16(b) making it possible for executives to exercise stock options and sell their stocks at the same time, thereby exploiting very short term movements in stock prices to their own advantage. Despite attempts to limit the amounts of tax deductible executive pay (Jensen & Murphy, 2004), other tax incentives encouraged stock options, as did the fact that corporations could avoid expensing options in their financial statements (Suchan, 2004).

Separation of Powers in Board Leadership

Often the CEO will sit on the Board of Directors for corporations in the United States. There is a growing corporate population calling for a clear split between executive leadership and board functions. The Separation of Board and Company, Jonathan F. Foster says that a Boards' most important function is to set an effective agenda that helps accomplish its primary objectives: "appointment, oversight and compensation of senior management; review of budgets and strategy; and oversight of financial reporting and capital structure." He goes on to say that an independent Board leader has the flexibility to set an appropriate agenda more easily than senior leadership and CEOs because they must focus on running the company, rather than running the board. Also, a CEO's immersion in the day to day operations may compromise her ability to maintain an objective oversight of senior management.

Given the limits to shareholder engagement, a key element of market oriented corporate governance is the presence of outside, independent members of the Board to represent shareholder interests. From the agency theory perspective, boards of directors and particularly independent or outside members are put in place to monitor managers on behalf of shareholders (Lynall, Goden & Hillman, 2003). The board of directors has the formal authority to ratify management initiatives, to evaluate managerial performance and to allocate rewards and penalties to management on the basis of criteria that reflect shareholders' interests. Agency theory suggests that a board comprised of independent directors for example board members who are not dependent on the current CEO or organization is more likely to provide an effective oversight of the firm's CEO and other executive directors. These arguments see board independence largely as a potential substitute for formal engagement by large shareholders. The evidence regarding the benefits of independent boards raises a question of why their effectiveness appears to be limited. Indeed, the failure of the Enron board to observe the warning signs as the company slid deeper into trouble remains something of a mystery. At least two issues are important in this regard. First, board members may not be sufficiently independent from the CEO (Bhagat & Black, 1999). Gilson (2006) describes the situation in the 1980s as follows, "The chief executive officer, rather than being selected by the board,

effectively selected who would be a director, and the shareholders passively endorsed the choice. The result was that directors saw themselves as advisers to senior management, not their monitors. If a director disagreed with the CEO's strategy, the proper response was the resignation of the director, rather than that the replacement of the CEO". More recently, Bebchuk (2005) finds that only a few of public companies in the USA faced contested board elections that were designed to get rid of existing directors. One of the barriers to contested board elections is associated with financial and organizational difficulties shareholders face when trying to place their own directors on a company's proxy statement. Bearing this in mind, Bebchuk supports suggestions that companies should be able to choose to provide shareholders with proxy statements via the Internet. This argument suggests the problem is that outside board members may remain insufficiently independent, particular since outside directors have little direct mandate to represent key shareholder or broader stakeholder constituencies. In the absence of stronger controls on the nominating process, most independent directors maintain a stance of "dysfunctional deference" to the CEO that limits their contribution of effective corporate governance (Sharfman & Toll, 2008). A second issue concerns the more inherent limits of independence. Outside directors may simply lack the amount and quality of information that insiders have. The information available may be too dependent on formal disclosure, too focused on finance rather than strategy and operations.

Directors' and officers' liability insurance

The wave of corporate scandals has resulted in a dramatic increase in shareholder class action suits and average settlement values. In addition, there is widespread concern that Sarbanes Oxley has made directors and officers more defenseless to lawsuits and liability with its Certification requirements, increased roles and responsibilities of directors, and the increase in the limitation period for bringing securities law violation suits. Directors' and officers' liability insurers have responded with increased premiums, reduced coverage limits, higher retentions, narrower coverage, expanded exclusions, restrictions on severability and multiyear deals. In Enron, Tyco and other recent cases, directors' and officers' insurers have sought to withdraw the policies and deny coverage on the grounds of misstatements in the applications. In order to protect, retain and recruit outside directors, companies are increasingly looking into purchasing 'individual' director liability insurance policies which provide coverage even when coverage becomes unavailable under the company's traditional directors' and officers' policy. These policies are non-rescindable except in the case of non-payment of premiums.

High-profile cases involving wrongdoing by corporate executives in the early 2000s intensified the exposure on how decisions made by those executives can impact a large number of people. For example, Enron Corporation, an energy company based in Houston, Texas, suffered a major collapse in 2001 that led to the largest bankruptcy in U.S. history. Acts of fraud on the part of corporate officers and others caused many of the problems. Employees of the company lost most of their retirement investments as a result of the company's collapse. Other companies, such as WorldCom, Tyco International, and Global Crossing, suffered similar fates. Both officers and directors of those corporations faced civil and criminal liability. Members of boards of directors for Enron and WorldCom agreed to pay millions of dollars out of their own pockets as part of settlement agreements. The U.S. Securities and Exchange Commission brought charges against top company officers, seeking to recover large fines in addition to criminal convictions. These incidents also led to major changes in federal securities laws regarding the potential liability for officers and directors.

Director recruitment and compensation

"The 1990s was the decade in which senior executive compensation shifted from being primarily cash based to being mainly stock based. With this change, management became focused not simply on the relationship between market price and breakup value which the advent of the bust up takeover compelled them to watch, but on the likely future performance of their firm's stock over the short term. Far more than the hostile takeover, equity compensation induced management to obsess over their firm's day to day share price." As late as 1990, the Business Roundtable, a group of chief executives of the largest firms, advocated the notion that "the directors' responsibility to carefully weigh the interests of all stakeholders as part of their responsibility to the corporation or to the long term interests of its shareholders." Yet by 1997, they argued that "the paramount duty of management and of boards of directors is to the corporations' stockholders; the interests of other stakeholders are relevant as a derivative of the duty to the stockholders" (quotes take from Fourcade & Khurana, 2009). The era of shareholder value had arrived.

The rise of shareholder value reinforced the "downsize and distribute" strategy of the previous decade dividend payout ratios remained high, downsizing continued despite the general economic recovery, and corporations remained focused on their core businesses. CEO continued to increase, while average wages stagnated (Hallock, 1998). Ideologically, organized labor no longer posed a great challenge to management and both unions and individual employees increasingly sought empowerment through the channel of pension fund ownership or employee share schemes. Still, the concept of shareholder value evolved and became infuse with range of new techniques of "speculative management" designed to influence company share prices, including road shows, stock splits, name changes, mergers, spin offs, changes to in company pension plans (Krier, 2005).

The increased time commitment being placed on directors has made director recruitment more challenging, particularly for companies seeking to fill an audit committee seat, where due diligence has become more extensive and two sided. Adding to the pinch in qualified candidates is the fact that sitting CEOs and directors are serving on fewer boards due to self-imposed restrictions and limits, suggested by the companies they serves. While the increased exposure and demands of directorship may warrant additional compensation, many boards have been reluctant to make significant changes given the critical focus of the press and shareholder advocates. However, an upward trend is evident, with the total annual package for an outside director approaching USD 250,000 at a few large blue chip companies. Most packages continue to have a cash and equity component, but stock options are being trimmed in preference of equity awards that emphasize long term goals, such as stock awards with long term holding requirements.

Absence of Employee Voice

A strong body of evidence now links employee voice in corporate governance to improved outcomes for employees and high productivity for companies. While the issue of stakeholder involvement remains controversial, the shareholder orientation of U.S corporate governance has been widely criticized by stakeholder theorists. What is less well known are the set of arguments linking increased employee involvement in the U.S. with improved functioning of various shareholder oriented mechanisms of corporate governance in the long term? In terms of shareholder engagement, union representation on pension funds has been associated with strong engagement on corporate governance issues. Union representation is not only a vehicle

for promoting employee interests, but also helps progress a number of agendas where employee shareholders and other shareholder have common interests avoiding excessive management pay, promoting transparency, assuring independent audits, etc. In terms of takeover markets, employee protection may help limit the scope of opportunistic strategies during takeovers, where new owners engage in breaches of trust to create short term gains. In terms of boards, experience has shown that employee representatives on the board of directors, either that elected via the workforce or appointed by unions; tend to be relatively independent of top management. Employee board members directly represent independent stakeholders and have access to information and knowledge of the employees, rather than being solely dependent on disclosure from management. While employees are often discussed as being company “insiders,” they are in fact quite independent relative to some “outside” board members who are essentially recruited by the top management. Similarly, debates on corporate social responsibility in the U.S. have long advocated the idea of “constituency directors” elected directly by shareholders to give weight to stakeholder interests (Brudney, 1982). In terms of managerial pay, **e**mployee representation on boards seem to have both more modest pay, but also more strictly defined long term performance criteria than in countries without employee representation (Buck & Shahrim, 2005, Fiss & Zajac, 2004, Sanders & Tuschke, 2006). Employees do not have an interest in avoiding incentivized or variable pay, but do have a strong interest in making sure such incentives are long term, consistent with the strategic goals of the organization, and compatible with the social norms of other employees in the firm.

Campaign Finance Disclosure:

With a Presidential Election in the United States in 2012, expect to see more pressure on directors to maintain oversight of corporate donations to political campaigns and adherence to proper campaign finance disclosures. According to a post by Francis H. Byrd called Top Ten Issues for Boards in 2012, "Taft Hartley and public pension funds are looking to increase the number of proposals they filed last year. Their hope is that the filed resolutions will lead to agreements with companies to limit and/or have the board oversee such contributions and corporate political activities." In house attorneys will want to keep tabs on the activities in this area and make sure that boards keep within the designated limits.

METHODOLOGY

Analytical and descriptive study method was used to understand performance of the principles and best practices of Corporate Governance and related problems in USAData collected were mainly from secondary sources through the use of internet searching and downloading the research papers related to the topic of the paper. About twenty research papers were downloaded and studied by the four researchers and gather the data after mutual discussion under the supervision of supervisor. The type of data was secondary data and source of data for this study is books and internet. The study has limitations of time constraint, access to limited libraries.

Objectives of Study

This study is to identify the problem related to Corporate Governance in United State of America and led us to a review of the existing literature related to corporate governance, including some recent problems.

- To establish the level of compliance with corporate governance guidelines and regulations by the organizations in USA

- To identify the relationship between corporate governance principles and problems of corporate governance in USA

Scope of Study

The study focused on problem of corporate governance issues in United State of America. The findings of this study will enhance the efforts of reader and researcher in coming up with corporate governance principles and guidelines that govern by the related department in any corporation. We gain immense knowledge aimed at creating awareness on corporate governance principles and guidelines for the benefit of the shareholders and all other stakeholders. The study will contribute to the achievement of the organization's policy of prosperity to benefit from properly run organizations and govern the corporations by correcting the problems of corporate governance.

The study will facilitate management by enhancing the knowledge of the board members. Good Corporate Governance practice provides a way to realize the idea of mitigating risk and optimizing performance simultaneously in competitive environment.

Corporate Miss-governance in USA

A collapse involves a major insolvency or bankruptcy of a failure. Following scandals were involving allegations of unethical behavior by people, acting within or on the behalf of a corporation. A corporate scandal sometimes involves accounting fraud of some sort. A wave of such scandals swept many United States companies in 2002. Some of the scandals of United States related to corporate governance after 2001 are given below.

Pacific Gas and Electric Company – 6 April 2001

It was Energy Company. After a change in regulation in California, the company determined it was unable to continue delivering power, and despite the California Public Utility Commission's efforts, it went into bankruptcy, leaving homes without energy. In 1998, a change in the regulation of California's public utilities, including PG&E, began. The California Public Utility Commission (CPUC) set the rates that PG&E could charge customers and required them to provide as much power as the customers wanted at rates set by the CPUC.

In the summer of 2001 a drought in the northwest states and in California reduced the amount of hydroelectric power available. Usually PG&E could buy "cheap" hydroelectric power under long term contracts with the Bonneville Dam, etc. Drought and delays in approval of new power plants and market manipulation decreased available electric power generation capacity that could be generated in state or bought under long term contracts out of state. Hot weather brought on higher usage, rolling blackouts etc. With little excess generating capacity of its own PG&E was forced to buy electricity out of state from suppliers without long term contracts. Because PG&E had to buy additional electricity to meet demand some suppliers took advantage of this requirement and manipulated the market by creating artificial shortages and charged very high electrical rates. The CPUC refused to adjust the allowable electric rates. PG&E Company (the utility, not the holding company) entered bankruptcy April 6, 2001. The state of California tried to bail out the utility and provide power to PG&E's 5.1 million customers, under the same rules that required the state to buy electricity at market rate high cost to meet demand and sell it at lower fixed price, the state also lost significant amounts of money.

WorldCom – 21 July 2001 [Telecomm]
CEO of WorldCom, Bernard Ebbers became very wealthy from the increasing price of his holdings in WorldCom common stock. However, in the year 2000 the telecommunications industry was in decline. WorldCom's aggressive growth strategy suffered a serious setback when, in July 2000, it was forced by the U.S. Justice Department to abandon its proposed merger with Sprint. By that time, WorldCom's stock price was decreasing and banks were placing increasing demands on Ebbers to cover margin calls on his WorldCom stock that were used to finance his other businesses. In 2001, Ebbers persuaded WorldCom's board of directors to provide him corporate loans and guarantees in excess of $400 million to cover his margin calls After falling share prices and a failed share buy back scheme, it was found that the directors had used fraudulent accounting methods to push up the stock price. Rebranded MCI Inc, it emerged from bankruptcy in 2004 and the assets were bought by Verizon.

As everyone now knows, events have moved swiftly in the days since that declaration. CFO Scott Sullivan, who was once regarded as an accounting wunderkind, has been sacked. The Securities and Exchange Commission has charged WorldCom with fraud. As the prospect of bankruptcy seems near-certain, Wall Street has punished WorldCom's stock, which was already in the pits even before the announcement; it closed at 10 cents on July 2. Analysts have warned that more bad news could be on the way, and that by the time the dust settles, WorldCom's failure could be more expensive than Enron's.

How did this happen? And even more importantly, how much confidence should investors place in companies' financial statements? According to experts from Wharton and elsewhere, accounting reforms are essential – but it will take much more than that to restore integrity and accountability in the corporate world.

"What's surprising about WorldCom is the very basic nature of what happened," says Karen Nelson, a professor of accounting at Stanford Graduate School of Business. "Enron was all about complex partnerships and accounting for special purpose entities. But what WorldCom did wrong is something that's taught in the first few weeks of a core financial reporting class. That's why people are asking, given its basic nature and its magnitude, how could it have been missed."

Enron – 28 November 2001 [Energy Company]
The Enron scandal, revealed in October 2001, eventually led to the bankruptcy of the Enron Corporation, an American energy company based in Houston, Texas, and the de facto dissolution of Arthur Andersen, which was one of the five largest audit and accountancy partnerships in the world. In addition to being the largest bankruptcy reorganization in American history at that time, Enron was attributed as the biggest audit failure. Chief Financial Officer Andrew Fastow and other executives not only misled Enron's board of directors and audit committee on high-risk accounting practices, but also pressured Andersen to ignore the issues. Directors and executives fraudulently concealed large losses in Enron's projects. A number of executives were sentenced to prison. This energy company created outside partnerships that helped it to hide its poor financial condition. It regularly misstated its earnings and assets, using a web of subsidiary and associate companies for the purpose. Executives paid themselves huge bonuses and also earned millions of dollars selling company's shares that were given to them at throw away prices as part of their remuneration package. The company eventually went bankrupt.

Shareholders of Enron lost USD 74 billion in the four years before the company's bankruptcy. As Enron had nearly $67 billion that it owed creditors, employees and shareholders received limited, if any, assistance aside from severance from Enron. To pay its creditors, Enron held auctions to sell assets including art, photographs, logo signs, and its pipelines. In May 2004, more than 20,000 former employees of Enron won a suit of USD 85 million for compensation of USD 2 billion pensions that was lost. From the settlement, the employees each received about USD 3,100. The next year, investors received another settlement from several banks of USD 4.2 billion. In September 2008, a USD 7.2 billion settlement from a USD 40-billion lawsuit was reached on behalf of the shareholders.

Arthur Andersen – 15 June 2002 [Accounting]
Arthur Andersen, based in Chicago, was a holding company and formerly one of the "Big Five" accounting firms, providing auditing, tax, and consulting services to large corporations. In 2002, the firm voluntarily surrendered its licenses to practice as Certified Public Accountants in the United States after being found guilty of criminal charges relating to the firm's handling of the auditing of Enron, an energy corporation based in Texas, which had filed for bankruptcy in 2001 and later failed. The other national accounting and consulting firms bought most of the practices of Arthur Andersen.

Adelphia Communications Corporation – 13 Feb 2002 [Cable TV]
Adelphia was the fifth largest cable company in the United States before filing for bankruptcy in 2002 as a result of internal corruption. Adelphia was founded in 1952 by John Rigas in the town of Coudersport, which remained the company's headquarters until it was moved to Greenwood Village, Colorado, shortly after filing for bankruptcy. The Directors of the company were sentenced to prison. The founders of Adelphia were charged with securities violations. Five officers were indicted and two (John Rigas and Timothy Rigas) were found guilty. Rigas founded Adelphia with a $300 license in 1952, took the company public in 1986 and built it by acquiring other systems in the 1990s. The company collapsed into bankruptcy in 2002 after it disclosed $2.3 billion in off-balance-sheet debt.

The majority of Adelphia's revenue-generating assets were officially acquired by Time Warner Cable and Comcast on July 31, 2006. LFC, an internet-based real estate marketing firm, auctioned off the remaining Adelphia real estate assets. As a result of this acquisition, Adelphia no longer exists as a cable provider. Adelphia's long-distance telephone business with 110,000 customers in 27 states was sold to Pioneer Telephone for about $1.2 million.

REFCO – 17 October 2005 [Brokering]
REFCO was a New York-based financial services company, primarily known as a broker of commodities and futures contracts. It was founded in 1969 as "Ray E. Friedman and Co." Prior to its collapse in October, 2005, the firm had over $4 billion in approximately 200,000 customer accounts, and it was the largest broker on the Chicago Mercantile Exchange. The firm's balance sheet at the time of the collapse showed about $75 billion in assets and a roughly equal amount in liabilities. Though these filings have since been disowned by the company, they are probably roughly accurate in showing the firm's level of leverage.

Refco Inc. entered crisis on Monday, October 10, 2005, when it announced that its chief executive officer and chairman, Phillip R. Bennett had hidden $430 million in bad debts from the company's auditors and investors, and had agreed to take a leave of absence. After

becoming a public company in August 2005, it was revealed that Phillip R. Bennett, the company CEO and chairman had concealed $430m of bad debts. Its underwriters were Credit Suisse First Boston, Goldman Sachs, and Bank of America Corp. The company entered bankruptcy and Bennett was sentenced to 16 years prison.

CONCLUSION

Major corporate problems and issues were included the issue of shareholder value, definition of independent directors, composition of the board, boards should have audit committee, appointment and re-election of directors, transparency, accountability, control, ethics, disclosure of audits, protection of shareholder rights, combined role of CEO and the chairman within the board and equity base pay of directors such as stock options. In the case stock options managers focus more of the rise of short term stock price in market and exercise their stock options. Taken as a whole, U.S. corporations have voluntarily pursued shareholder friendly policies in the 1990s. We believe management's acceptance of the shareholders' perspective was greatly aided by profitable stock option plans, which allowed executives to reap big financial gain from increased in share prices. The focus was on forcing corporate assets out of the hands of managers who could not or did not want to use them efficiently. The results included takeovers and restructurings of companies with excess capacity.

The move towards shareholder and market preeminence is apparent in the way corporations have reorganized themselves. There has been a broad trend towards decentralization. Large companies are trying hard to become quicker and to find ways to offer employees higher powered incentives. At the same time, external capital markets have taken on a larger share of the reallocation of capital. Corporate managers still reallocate vast amounts of resources in the economy through internal capital and labor markets; the boundary between markets and managers appears to have shifted. As managers have given up authority to the markets, the scope and independence of their decision making have narrowed.

Corruption is out of control throughout the world. Evidences show that basically there are two causes of corruption namely: greed and need. While needs can be met by reviewing pay packages, etc, no package can take care of the greed which has no end. As a consequence of moral bankruptcy and consequences of devaluation of man plaguing practically all including developing and developed countries there is an increasing tendency to channel funds to get rich too soon to maintain unproductive/ non performing assets.

Having addressed where the U.S. system is today and how it got there, we finally consider the probable near term effects of the legislative, regulatory, and market responses to the perceived corporate governance problem. We conclude that the current changes are likely to make a good U.S. system a better one, although not without imposing some unnecessary costs. In fact, the greatest risk now facing the U.S. corporate governance system is the possibility of overregulation. How could an inefficient governance system produce so much wealth? And what about all the family firms that became conglomerates? Family firms are subject to fewer agency problems than widely held companies, yet many of them followed the general trend. Capital markets have come to play a bigger role not because they have become better at allocating resources and not because managers misbehaved, but rather because the market's comparative advantage has been favored by economy wide trends in deregulation, globalization, and information technology. If the shifts in corporate governance have been

driven by these factors, then the market's strong influence on corporate governance may be more transitory.

Employees know that their firm specific knowledge is likely to become less valuable once the firm changes course and starts pursuing new lines of business. A new firm, with a lack of commitments and old baggage, can offer a distinctive competitive advantage in rapidly growing industries. From this perspective, forcing older companies to adhere more rigorously to maximization of shareholder value reduces those activities of employee influence that cause costly delays, distorted investment decisions, and misguided efforts to save jobs. If decisions of where to cut and where to expand jobs were left to a democratic body of workers, the heterogeneity in employee preferences would make the process of change slow and costly.
U.S. corporate governance has changed substantially in the last 20 years. The underlying substance of this transformation has been that U.S. managers have become much more focused on stock prices. We have argued that at least some of the efficiency gains associated with these changes can be traced to the comparative advantage of markets in undertaking large scale change. Since these effects are temporary, it is possible that the current level of market influence on the governance and organization of firms is going to decrease.

SUGGESTIONS – HOW TO SOLVE THE IDENTIFIED PROBLEMS

1. Companies must comply with applicable governance related provisions required by the Sarbanes Oxley Act of 2002, related regulations of the Securities & Exchange Commission (SEC) and applicable listing standards as well as with all other applicable laws, regulations, and company articles and bylaws. For example, it is assumed that most publicly traded United States corporations those that do not qualify for certain controlled company exemptions now have a majority of independent directors; that independent directors hold periodic executive sessions without members of management present; that such sessions are convened and presided over by an independent director chosen by the independent directors; and that audit, compensation, and nominating/governance functions are undertaken by independent directors usually organized in committees. The Key Agreed Principles that follow are grounded in the common interest of shareholders, boards, and management teams in the corporate objective of long term value creation through ethical and legal means, the accountability of management to the board, and ultimately the accountability of the board to shareholders for such long term value creation. The Principles provide a framework for board leadership and oversight in the especially critical areas of strategic planning, risk oversight, executive compensation, and transparency. First; principle emphasizes the responsibility of every board to design its own governance structure and practices, and secondly, principle emphasizes the importance of the board explaining how it has tailored governance structures and practices to meet its own needs. Thirdly, principles describe the key fundamentals that boards should take into account in designing and explaining structures and practices.
2. Governance structures and practices should be designed by the board to position the board to fulfill its duties effectively and efficiently. The board of directors, as the central mechanism for oversight and accountability in corporate governance system, is charged with the direction of the corporation, including responsibility for deciding how the board itself should be organized, how it should function, and how it should order its priorities.
3. The board's fiduciary objective should be long term value creation for the corporation; governance form and process should follow by the boards.

4. Shareholders and management should have important viewpoints about governance structures and processes, and shareholders elect directors and have authority for certain critical decisions.
5. Boards should take extra care with selecting and evaluating senior executives, planning for succession, monitoring performance, overseeing strategy and risk, compensating executives, approving corporate policies and plans, approving material capital expenditures and transactions not in the ordinary course of business, ensuring the transparency and integrity of financial disclosures and controls. Board should provide oversight of compliance with applicable laws and regulations and the board must decide how best to position itself to fulfill its fiduciary obligations.
6. The NYSE rules require boards and core board committees to perform annual self-evaluations. While the idea of group and peer evaluation has typically been acknowledged with mixed feelings by directors, it is expected that many boards will begin to see these evaluations as an opportunity to improve board and committee process to optimize their approach to strategic planning, goal setting and monitoring. Boards should begin to rely more heavily on outside consultants, who can help to guide the evaluation process to make it as trouble-free and productive as possible.
7. Corporations should facilitate and encourage the weak and dispersed shareholders to attend the board meetings by arranging the board meetings at nearby city of these shareholders and paying travelling expenses to them. This will lead to more participation of shareholders and can provide corporations more opportunity to gather the ideas for the improvement of the organizations.
8. Financial accounting audit firms should be changed after specific period of time. Similar accounting audit firms do audit repeatedly in same corporation can develop relations with the management of corporation and can lead to hiding accounting facts and can causes corruption.
9. Accounting audit firms should be well reputed, honest and fair. There should be no evidence of even a minor scandal and involvement of that accounting audit firm in any fraudulent or corruption.
10. Directors are a company's soul and we agreed with the Chinese saying, "Water can carry a boat; it can also sink a boat" applies. They have to understand the nature of the trust shareholders place in them and not for one moment pronounce free from blame themselves of the fiduciary duties. We believed that independent non-executive directors played a pivotal role in overseeing the internal control and financial reporting systems of issuers, and providing checks and balances over the board's decision making on significant transactions.
11. For professional advisers, their privileged position carries with it special responsibilities. The professions had to demonstrate their ability to monitor adherence of their members to professional and ethical standards. Any self-regulatory regime has to be effective, transparent and accountable.
12. Free flow of information through the media has been vital to both our own healthy market development and the confidence of overseas investors in our market, the media also has a particular responsibility for the fairness and accuracy of the information and the assessments it publishes.
13. Shareholders, as owners of companies, should have a legitimate interest in how their company behaves; and legitimate rights in expressing their views. "Empowering them and facilitating their exercise of their rights are indispensable elements of ensuring good corporate governance.
14. Board composition should relate to the company’s strategic needs, which change as a company and its business environment evolve. Shareholders and key constituents are interested in the value that diverse perspectives bring, including those related to gender and racial diversity.

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