3 Factors That Contribute to Good Corporate Governance

Description

As financial markets become more efficient, it becomes increasingly difficult to gain an edge and outperform the competition.

Lately this has led to a renewed focus on the corporate governance practices employed publicly traded companies.

Most financial experts are in agreement that companies with sound and transparent ethics and principles tend to enjoy more sustainable business models, a more positive corporate culture and improved employee engagement.

The three factors listed below will give you a head start in understanding whether your company is following best practices related to the corporate governance of publicly traded companies.

The chairman of the board is independent of management

This is one of the oldest, but more important contributors to good corporate governance.

To take it back a step, the job of the board of directors is to manage the relationship between a company's shareholders (its owners) and the management (the people responsible for managing the day-to-day operations of the company).

It's a relationship that needs to be managed carefully because it's the owners who are responsible for paying the employees salaries. Meanwhile, however, the owners aren't there to oversee the employees to make sure they're doing their jobs.

Having an independent chairman (someone who isn't an employee of the firm) is a big step in ensuring that shareholder's rights are being looked after.

Thankfully, most companies do follow this practice today. However, not too long ago, **Magna International Inc.** (TSX:MG)(NYSE:MGA) founder Frank Stronach jointly held the title of CEO and Chairman.

Independent committees

In addition to the company's chairman, the board of directors will also include certain committees, such as a committee to oversee financial reporting in addition to executive compensation.

As is the case with the role of the chairman, it's also important that at least the majority of these committee members remain independent from company management.

After all, it wouldn't make much sense to have members of senior management in a position to influence their own compensation packages?

Avoid companies with "anti-takeover" measures

Maybe you're new to investing. Maybe you didn't know that sometimes the most profitable investments are those in which the company you own has merged with a larger company.

These scenarios can be very lucrative, as the takeover prices paid for publicly traded companies are often at a sizeable premium, sometimes 20-50% over their share prices or more, as was the case when **Aurora Cannabis Inc.** (TSX:ACB) acquired MedReleaf earlier this year.

Generally speaking, takeovers are a good thing; you'll want to be on the lookout for companies with anti-takeover mechanisms in place, like "poison pills" or "golden parachutes."

Those types of measures are designed to protect the interests of management, not shareholders.

Bottom line

If you see yourself as a long-term investor in a company, you're going to want to make sure you're placing your hard-earned capital with a company you can trust.

Follow these three tips to ensure the companies in your portfolio are doing the right thing – and following good corporate governance practices.

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