Opinion

10 REASONS TO CONSIDER CORPORATE GOVERNANCE

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1. Institutional shareholders consider it highly relevant to their interests as shareholders. Given their greater opportunity for coordinated action and their substantially larger holdings than those of individual shareholders they differ from individual shareholders in exercising their shareholder rights more aggressively. Simply because individual shareholders may acquiesce in the behavior of a corporate board does not mean their advisors should do so.
2. Historically conventional mutual fund management companies –perhaps in response to the interest of institutional shareholders—are beginning to organize funds, where the portfolio manager[s] consider the corporate governance policies and practices of companies they consider for potential investment. Examples include Thornburg and Matthews Asia.
3. Investors are entitled to demand that boards of directors give highest priority to the investors' interests. Investors know that in other contexts such as governmental institutions and non-profit organizations the entities perform more effectively, efficiently, and responsively, if investors acting as citizens or participants in communities served by non-profit organizations demand accountability in accordance with a fiduciary standard of behavior. Why demand less with regard to for-profit entities simply because it may be difficult to coordinate action with other investors?
4. Morningstar has begun to rate mutual funds based upon sustainability factors including corporate governance. Most corporations are presumed to be entities that will survive without time limit. Especially in an era of climate change and related societal disruption how can a corporation be presumed to be perpetual, unless the board of directors performs its fiduciary duties highly responsibly and responsively?
5. Institutions including for-profit corporations that are not highly alert to competitive threats and other sources of disruption to the business/operating model of the institution/corporation are not likely to survive long much less in perpetuity. The capitalist model that assumes a constant threat of mergers and acquisitions reinforces the threats to the continuity of a for-profit corporation. These dynamics demand a highly functioning board of directors with a strong sense of fiduciary duty to investors. Corporate governance matters to a corporation's survival.
6. Current corporate behavior illustrates how corporate governance matters. The best current example is Volkswagen, where the concentration of voting power allowed recent company CEOs to pursue strategies including circumvention of environmental and financial regulatory requirements without adequate, timely accountability to the board of directors and company investors. The financial damage to the company remains difficult to assess, but presuming that the company will remain in perpetuity may be misplaced, which is shocking for a company of such market scope and political power.
7. There are many other examples of corporate demise or near demise attributable in substantial part to the failures of boards of directors to perform their fiduciary duty satisfactorily. Ones that come readily to mind are Hewlett Packard [acquisitions that had to be written off because of failures of due diligence prior to acquisition], Procter & Gamble [failures in selection of CEOs, who proposed poorly conceived acquisitions or lacked the managerial skills to divest assets timely], Kinder Morgan, Inc. [poorly timed and highly leveraged rollup of limited partnerships into C corporation], Energy Transfer

Partners [poorly timed proposed merger with Williams Companies], Bombardier [overly ambitious and too highly leveraged effort to compete with Boeing and Airbus that has nearly bankrupted the company], Penn Central [poorly conceived merger of the New York Central and Pennsylvania Railroads], Hughes Tool [failure of board of directors to oversee poorly conceived and executed activities of CEO], and even General Electric [failure of board of directors to oversee CEO, who was lionized by the business and other media and extended the scope of the company's financial services activities so far that the company became too heavily dependent upon the functioning of the commercial paper market]. The list could go on.

8. The decline in assets of the larger, actively managed mutual fund management companies and the associated rise in assets of the prominent marketers of exchange traded index funds, also, may be attributed in part to the failure of the portfolio managers at the active managers to analyze companies' corporate governance prior to investing in the companies. Few conventional [non-ESG] fund managers consider corporate governance as an integral part of their portfolio management process. This omission undermines the ability of such managers to demonstrate value to fund investors, who opt to invest in index funds that [with few exceptions] are agnostic about corporate governance. [A few ETFs do incorporate ESG factors into the design of the index that the ETF mimics.] Perhaps in their effort to demonstrate value relative to ETF competition more active fund managers will recognize the potential competitive advantage of considering the corporate governance of the companies within their fund portfolios.

9. Climate change creates multiple new sources of operational and financial risk for public corporations to manage. The societal disruption associated with climate change is surprising and will continue to surprise many individuals including CEOs and boards of directors. Especially if the pace of disruption accelerates many boards of directors will be hard pressed to perform their fiduciary duty in an adequately timely and knowledgeable manner. Investors will have reason to care about how boards of directors respond to the many challenges of climate change to the assumption that corporations operate in perpetuity.

10. In the current era when in this country and elsewhere there are many variables at work that contribute to the disruption of societies it is apparent and will become more apparent that many political leaders lack/will lack the wisdom, perseverance, and character to manage well social, economic, and political problems. In this context it will be even more important that the boards of directors of corporations demonstrate the wisdom, perseverance, and character that many political leaders lack/will lack. This is illustrated in connection with the societal discussion of climate change. Some business leaders have the intelligence and courage to address the threats to their businesses from the impacts of climate change and the investment opportunities associated with participating in the mitigation of climate change. They recognize that climate change presents both existential threats to their corporations [including their employees and physical assets around the world]and creates a demand for mitigation solutions that can be highly profitable for their corporations. Corporations with the best corporate governance are more highly likely to meet the challenges. Investors will have a keen incentive to know which are these companies.

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