



Why good corporate governance still matters in private companies

Listed companies may look enviously at their privately owned counterparts, which typically have fewer regulations to worry about. But, as *David Burrows* discovers, following the principles of good corporate governance is vital for private companies to thrive.

Discussion of corporate reporting typically centers around those companies that are listed on a stock exchange. In an era when social media and online research capability means that news (whether good or bad) travels fast, quoted companies are increasingly aware that the onus on them to be transparent and accountable is greater than ever.

Shareholders and other stakeholders are now able to keep tabs on companies like never before. Moreover, issues such as sustainability and ethical standing now sit alongside traditional measures of financial strength and market position as factors that are indelibly tied into investment decision-making.

But what about private companies, whose shares are not in public hands? They may not be accountable to a vast array of stakeholders, but good corporate governance is still important. Just because a company is private doesn't mean it isn't accountable to its workforce, suppliers, partners and customers, as well as society as a whole and the environment. There may not be a share price to worry about, but there are plenty of other concerns.

EY Reporting spoke to the finance leaders of two private businesses to find out how they approach the key elements of corporate governance and what they see as the advantages (and disadvantages) of not being listed.

Subtle differences

Don Solman is CFO of James Richardson & Sons, Limited, a family-run corporation based in Winnipeg, Canada that owns businesses in sectors including agriculture, financial services, real estate and oil and gas. He explains that the obligations listed companies in Canada are subjected to – which largely mirror those in the US and the UK – are subtly different to those faced by private businesses.

"With public companies, a lot of time is taken up dealing with statutory requirements," he says. "The fact that we, as private companies, are not subjected to the same requirements does not abdicate us in any way from good corporate governance. However, we are not subjected to the same level of form-filling."

Alaaeldin Shousha, Director, Finance and IT at Saudi Arabia-based Sunbulah Group (a privately owned food manufacturing company), agrees that there is no abdication of good corporate governance in a well-run private business. Indeed, he maintains that demands on the CFO of a private company only differ marginally from those that their counterpart in a public organization has to deal with, and gives short shrift to any suggestion that the role of a public company CFO is more about compliance with legislation.

"In my case, I don't really see any difference," he says. "Other than publishing financial and investor information on government and company websites, we have the same IFRS reporting requirements."

But is there a danger that private companies that disclose less financial information risk therefore being perceived as less open or trustworthy than listed businesses?

"I would have agreed with this statement before 2017," says Shousha. "However, all companies, listed and private, are now required to follow IFRS reporting and international auditing standards, with very minor exceptions."

In Sunbulah Group's case, the preference is to issue quarterly financial statements – despite the additional cost and the fact that they are in no way mandatory. Shousha explains that regular quarterly reports show how different sectors of the business are performing. He argues that this level of transparency has helped to establish trust with debtors and made it easier to secure extended credit terms.

"Following the best practice of corporate governance engenders the trust of investors and debtors in the group. This also allows us to be viewed as a solid and well-established partner in our joint ventures, both inside and outside the Kingdom," he stresses.

Shareholder relationships

As for shareholder pressures, Solman insists they still exist for private firms, and to some extent are greater than for public companies. "The nature of a private company means I look in the shareholders' eyes on a regular basis," he says. "In a public company, those shareholders are 'faceless' and nowhere near as engaged in the business." In short, with a private company the relationship tends to be far more open and immediate.

There is also flexibility for private companies in not always having to appease the short-term demands of public shareholders. Solman makes the point that a private company could make a

“

The nature of a private company means I look in the shareholders' eyes on a regular basis.

Don Solman

James Richardson & Sons, Limited

business decision or transaction that might not be beneficial in terms of earnings per share until a later time. A move of such foresight might not be so easy for a listed firm. He adds: "As a private company, we don't have to think about sending a story to the market to ensure our share price moves in a certain way."

And not only is decision-making less pressured, it is also typically more direct. Private companies are nimble in terms of making operational and growth strategy decisions without needing widespread shareholder approval. "I can walk into the CEO's office with an idea, which, if approved, I can implement immediately," says Solman. "Not only can we act quickly, but our competition doesn't know what our plans are, since we don't have to share any information with the public."

This ability to keep certain information in-house is something Shousha also mentions. "We enjoy the confidentiality of internal records by not announcing the board of directors' decisions and resolutions to the outside world," he says.

By way of example, he points to a recent board resolution that was required to make an offer for a rival business. Unlike a listed company, which would have had to make its takeover intentions public via a stock exchange announcement, the Sunbulah board were able to keep their plans under wraps. "Public companies are obliged to provide such data," Shousha adds, "and this information could then be used by others who might then hunt the deal."



The benefit to private companies of these rules, as Solman points out, is that they are able to analyze reports released by their publicly owned counterparts – but this doesn't apply the other way around. "Essentially, it means we often know more about them than they know about us," he says.

Adopting a UK approach

A significant recent development in private company governance was the introduction of the Wates Corporate Governance Principles for Large Private Companies in the UK. Under these principles, businesses are required to make a statement on their corporate governance arrangements for financial years beginning on or after 1 January 2019, under six headings: Purpose, Composition, Responsibilities, Opportunity and Risk, Remuneration, and Stakeholders. Is this approach something that would be welcomed in other countries?

From a Canadian perspective, Solman has reservations. "If it helps our shareholders manage our business better, then yes, but I'm not sure all of those factors do that," he says. "The danger is that it could just be a box-ticking exercise."

Shousha would broadly welcome such principles in Saudi Arabia. "I can assure you that our group will happily follow the mandates as stated above without any restrictions."

Family affairs

Many private companies are run by families and passed down through the generations – although, as Solman points out, one of the risks for such companies is that it is rare that they last for multiple generations. The business model is often reliant on someone in the family checking that good senior management decisions are made. What if a family member at the helm is not open to new ideas, lacks vision or is not vigilant in maintaining the highest standards of corporate governance? In this situation it is up to other family members to provide the necessary checks and balances and make certain that the business is operated as the collective family desires. Without this, it can be difficult to sustain the business over the generations.

According to Shousha, the way to keep the family business model working efficiently is by implementing a suitable structure for the board. "At Sunbulah, we have just two family members – the Chairman and Vice-Chairman – on the board. The remaining five board members are fully independent. I like private companies to be structured this way."

What does good look like?

Whether a company is private or public, the smooth running of the business ultimately depends on the quality of the team and the processes in place. It is not a case of one being better than the other. While there are disadvantages to being a

family-owned business, as Solman points out, the owners of such a company frequently offer value that senior executives at a public company do not. For example, those executives typically leave on a fairly regular basis – their ties to the business are not as deep-rooted.

And, while private companies may not be subjected to exactly the same requirements as listed names, what is deemed good practice in general is largely embraced on both sides of the fence. As Solman concludes, it is not a case of calculatedly copying the corporate governance practices of public companies with an eye on becoming listed one day; it is more about identifying good practice and implementing it as a matter of course. ■

July 2019



Profile: Don Solman

Don Solman is Vice-President and CFO of James Richardson & Sons, Limited (JRSL)

a privately owned and operated Canadian corporation based in Winnipeg. He took up the post in February 2015, having previously been Executive Vice-President and CFO of Richardson International Limited, JRSL's largest operating subsidiary. He is a member of the board of directors of six of JRSL's subsidiary companies. A graduate of the University of Manitoba Asper School of Business in Canada, he received his Chartered Accountant designation in 1985 and was awarded his FCA in 2016.



Profile: Alaaeldin Shousha

Alaaeldin Shousha is Director of Finance and IT at Sunbulah Group, a privately owned food manufacturing

company based in Jeddah in Saudi Arabia. As well as managing the finance and IT functions, he leads on business planning, strategy and M&A activities. He joined Sunbulah in August 2015, having previously performed senior finance roles at Mondelez International (2011-2015) and Kraft Foods Europe (2008-2011); both posts were based in Zürich, Switzerland. He has a Bachelor of Business Administration degree from Helwan University in Cairo, Egypt and an Accounting Diploma from the Kraft Foods Finance Academy.

EY | Assurance | Tax | Transactions | Advisory

About Reporting

Reporting, EY Assurance's insights hub, brings together insights and ideas that will interest, inform and inspire business leaders. It's about more than the numbers, examining reporting in its broadest sense.

Our content is tailored for board members, audit committee chairs and finance directors of global companies. For more information, visit ey.com/reporting.

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via ey.com/privacy. For more information about our organization, please visit ey.com.

© 2019 EYGM Limited.
All Rights Reserved.
EYG no. 003062-19Gbl
ED 0720

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax or other professional advice. Please refer to your advisors for specific advice.

The views of third parties set out in this publication are not necessarily the views of the global EY organization or its member firms. Moreover, they should be seen in the context of the time they were made.

ey.com