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Reflections on Corporate Governance following Clerys’ closure

The sudden closure of department store Clerys in June 2015 raises some interesting corporate governance issues.

By way of background, Clery’s is a department store in Dublin’s main street, O’Connell Street. Until recently it was a family-owned business, having been established in 1853. It has a particular place in Dubliners’ hearts, as many courting couples would arrange to meet under Clery’s clock.

In 2012, Clerys was purchased by a Boston-based US firm of turnaround experts, Gordon Brothers, for €14 million.

Fair play to Gordon Brothers. It sold the fine building on O’Connell Street housing the Clery’s trading business to a property investment consortium, Natrium, for a reputed €29 million, making a tidy profit of €15 million in three years. I think they call it shareholder value!

The purchaser, Natrium, is co-owned by chartered accountant Deirdre Foley’s D2 Private and a London-based fund manager, Cheyne Capital.

I will mention in passing that chartered accountants (of which I am one) as professional people are subject to strict ethical and moral codes of conduct at the heart of which is a duty beyond one’s own interests to the public interest.

Is this legal?

What appears to have happened is that the property on O’Connell Street was moved by Gordon Brothers, out of the trading company into a separate company and was then sold on to Natrium. Minus its main asset, the trading company, could not continue to operate as a going concern and had to immediately be put into liquidation.

The conduct of company directors is mainly a matter for common law or judge-made law. It is a fundamental principle of common law that directors’ duty is to look after the best interests of their company. Under common law in Ireland, directors owe their duty to the company as a whole, not to individual shareholders or classes of shareholders under the principle established and pithily articulated in the 1902 judgment Percival v Wright “Directors have but one master, the company”. More recently, the principle has been enshrined in statute in the Companies Act 2014.
Generally, if directors look after the best interests of the company, the company's shareholders will benefit. Thus, the distinction between looking after the interests of the company and shareholders in most cases has no consequences in practice. However, in extreme cases, where directors focus on shareholders/shareholder value (in modern capital markets this is often an excessively short term perspective), they may 'kill' the company through misplacing their duty to shareholders instead of to the company. Thus, duty to company (rather than its shareholders) implies a longer-term perspective and a requirement for prudence in ensuring the survival of the company.

The Clery's property transaction appears to me to be such an extreme case.

I cannot understand how directors moving the main property asset out of the trading company, resulting in its immediate closure, could be construed as acting in the best interests of their company.

**Shareholder value versus stakeholder value**

While Gordon Brothers shareholders have made millions in flipping Clerys in a three year period, approximately 460 Clery's employees have lost their jobs.

Another debate in corporate governance is whether companies should be run solely for the purpose of generating shareholder value or whether a broader stakeholder value perspective should be taken, whereby the interests of stakeholders such as employees, customers, suppliers are also considered.

In the US, businesses are operated with a hard-nosed shareholder value perspective. We Europeans adopt a more stakeholder value perspective.

Under Irish company law, directors owe their duties first to the company, then to shareholders ("members as a body"), and then to stakeholders, of which two groups are mentioned in company law: creditors and employees. When a company approaches insolvency, the duty to the company alone is effectively transposed into a duty to act in the interests of the company's creditors. Clerys' creditors might wonder at whether the directors have complied with these legal provisions.

Directors also have a statutory duty to have regard to the interests of employees. Directors' duties to employees are subsidiary to their duties to the company, as the duty to employees is owed to the company. It is the interests of the company which must ultimately be paramount. This provision is also reflected in the Companies Act 2014, as follows:

> Directors to have regard to interests of employees.

**224.** (1) The matters to which the directors of a company are to have regard in the performance of their functions shall include the interests of the company's employees in general, as well as the interests of its members.
(2) Accordingly, the duty imposed by this section on the directors shall be owed by them to the company (and the company alone) and shall be enforceable in the same way as any other fiduciary duty owed to a company by its directors.

Concluding comment

Reading about the Clerys’ transaction leaves a bad taste in one’s mouth. Well done to those who have been raising a stink about it. There is some justice in seeing the reputational damage suffered by Gordon Brothers, Deirdre Foley and her D2 Partnership and Cheyne Capital. We need people with a high sense of social justice, who know the difference between right and wrong, to act as company directors.