Corporate Restructuring: A Primer

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Abstract: The Covid-19 pandemic was perhaps one of the most challenging eras for companies to continue thriving. Within an instant, lockdown measures had been imposed and thousands of companies across the globe shut down. However, the businesses that were able to restructure themselves within a reasonable time, such as the shift from physical to virtual mode, survived the pandemic. Survival in a competitive environment is perhaps the decisive factor for a company to reorganize its legal structure at certain intervals. 'Synergy' may be defined as an amalgamation, interaction, or cooperation between 2 or more companies, to produce a ripple effect greater than the sum of their separate effects. In short, 2 plus 2 must equal 5. There are several modes of restructuring from which companies hope to benefit, such as mergers and acquisitions, joint ventures, strategic alliances, demergers, etc. In this paper, the author has delved into the various modes of corporate restructuring that have been adopted by businesses over the years. To better explain the concept, the author has taken up a plethora of live cases and illustrations.

Keywords: *Corporate restructuring, Synergy, Merger, Acquisition, Demerger.*

1. INTRODUCTION

The term 'Corporate restructuring' essentially refers to a change in the business structure or operations of a company, undertaken to ward off financial instabilities. Amid a dynamic business environment, it is but natural that a company may not be able to keep up with customers' demands, and thereby run into losses. In such instances, companies usually reorganize their business setups to eliminate disadvantages combine advantages, and achieve synergy benefits through trailblazing strategies.

In the yesteryears, business reorganizations were taken up only in instances when the company encountered financial troubles. For instance, in the event of a company being unavailable to pay a corporate debt, it would enter into a restructuring clause with its creditors. In that clause, the restructuring procedure and the company's strategy to pay off the debt would be mentioned. However, today, restructuring is not merely considered an option, but a

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conscious effort undertaken by shareholders to improve their company's competitive position and survive blips in the market environment.

2. Why is Corporate Restructuring undertaken?

2.1. Increase in market share

Mergers and acquisitions involve an interaction between 2 or more companies, and therefore, there is an increase in the market share of the entire unit. Such market share is achieved by providing customers with additional goods and/or services. A horizontal merger, i.e., an amalgamation of 2 companies engaging in competing services, is indispensable to increasing market share. For instance, a merger between Coca-Cola and Pepsi would be a horizontal merger and would reap a greater market share.

2.2. Reduced competition

One of the foremost aims of a horizontal merger is to reduce competition. On September 3, 2001, HP and Compaq announced a 25-billion-dollar merger agreement.[1] While several naysayers and HP and Compaq partners feared a painful and even disastrous integration, the merger was a significant success. The merger helped the companies establish a technology powerhouse, with dominant revenue positions in servers, printers, and PCs. In a statement made to CRN, HP claimed that the merger helped the 2 companies to produce greater, and much faster than either company could have individually.

2.3. New technology

Rapid technological development is what defines today's world. Therefore, companies must keep track of technological advancements and reorganize their business structures in consonance with the status quo. Companies employing unique technologies in running their businesses are more likely to have a competitive edge over others.

Starbucks, a global coffee chain, is one of the best examples of a company keeping pace with today's dynamic digital landscape. The road to attaining a household name was not without challenges; in 2008, Starbucks was hit with a severe financial crisis that caused it to close down almost 1,000 stores and experience a net profit loss of 28% over the next couple of years. However, rapid reorganizations and new strategies based on technology, community involvement, and free thinking have ensured unimpeded growth into new markets.[2] For instance, reinforcement learning is a kind of machine learning technology that enables people using the Starbucks app to

[1] Rob Wright, 'The HP-Compaq Merger: Partners Reflect 10 Years Later' (*CRN*, 8 September 2011) <https://www.crn.com/news/mobility/231601009/the-hp-compaq-merger-partners-reflect-10-years-later.htm> accessed 10 February 2023

[2] 'Delivering an Effortless Coffee Experience through Physical and Digital Integration' (*Geospatial World*, 4 March 2022) <https://www.geospatialworld.net/prime/case-study/location-and-business-intelligence/delivering-an-effortless-coffee-experience-through-physical-and-digital-integration/> accessed 10 February 2023

receive customized recommendations. Starbucks also uses IoT to carefully keep track of the performances of its products; it analyses data such as the type of beans, the coffee temperature, and the water quality.

2.4. Diversification

The cooperation of 2 companies running completely unrelated businesses leads to greater diversification and thereby helps attract a larger customer base. It also reduces risk, for if one of the businesses fails, the other one could come to the rescue of the shareholders. The 1995 merger between the Walt Disney Company and the American Broadcasting Company (ABC) is an apt example of a conglomerate merger, since the former is an entertainment company, while ABC is a broadcast television network. Through this merger, Disney gained access to ABC's national television realm and ESPN's widespread sports coverage.[3]

2.5. Strong brand

It might take several years before a company can garner a reputation on its brand name. Therefore, companies prefer acquiring established brands, to increase their customer base within a short period. In 2008, Tata Motors acquired Jaguar Land Rover for 2.3 billion US dollars. Both Jaguar and Land Rover were iconic British brands at the time of the acquisition, and therefore, Tata Motors capitalized on the 2 brands' commercial potential.[4]

3. Modes of Corporate Restructuring

3.1. Mergers and Acquisitions

While the terms 'Merger' and 'Acquisition' have often been used interchangeably, they are significantly distinct. A merger refers to a combination of 2 or more companies, who decide to surrender their stocks and formulate a joint organization. For instance, in 2000, America Online (AOL), the largest internet provider in the US, merged with mass media and entertainment conglomerate, Time Warner Inc. (TNW). With attaining dominance in the market is one of the foremost reasons for mergers, the 2 giants aimed at creating a formidable force in the Internet, cable, music, publishing, and entertainment industries.[5] On the other hand, acquisition occurs when a company takes over another and establishes itself as the new owner. A major difference between a merger and an acquisition is

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[3]Geraldine Fabrikant, 'The Media Business: The Merger; Walt Disney to Acquire Abc in $19 Billion Deal to Build a Giant for Entertainment' (*The New York Times*, 1 August 1995) <https://www.nytimes.com/1995/08/01/business/media-business-merger-walt-disney-acquire-abc-19-billion-deal-build-giant-for.html> accessed 10 February 2023

[4] 'How Ratan Tata Brought Life to Jaguar Land Rover - the Deal Came at a Worse Time' (*The Economic Times*,18 March 2018) <https://economictimes.indiatimes.com/industry/auto/auto-%20news/how-ratan-tata-brought-life-to-jaguar-land-rover/triumph-over-humiliation/slideshow/63245739.cms> accessed 10 February 2023

[5] 'History Moment in Media: AOL Time Warner Merger' (*Media Village*, 14 January 2019) <https://www.mediavillage.com/article/historys-moment-in-media-aol-time-warner-merger/> accessed 10 February 2023

that in the former, one or more companies are dissolved to establish a new one, while in the latter, no new company is either created or destroyed.

The concept of synergy implies that the combined efforts of 2 or more entities are more efficient and profit-making than the efforts of a single entity. Both mergers and acquisitions involve a combination of the resources of the companies, such as managerial skills and production facilities. The amalgamation of operations breeds integration, which in turn increases earnings potential and reduces cost. The success of synergy could be on account of several factors, such as simplification of processes, the rise in productivity, focused operational efforts, and better procurements.

3.1.1. Types of Mergers: Horizontal and Vertical

The term 'merger' has usually been associated with an amalgamation of 2 competing companies, who agree to create a joint organization to use their resources in a more lucrative manner. One of the best examples of a horizontal merger is the integration of Facebook, Instagram, WhatsApp, and Messenger. One of the major reasons why the social media companies decided to merge with WhatsApp was to utilize the end-to-end encryption technology, for protecting user privacy.[6]

A vertical merger, on the other hand, is an amalgamation of 2 or more companies, that are not in a direct line of competition but exist in the same supply chain. For instance, an automobile company merging with a parts supplier would constitute a vertical merger. One of the most famous examples of a vertical merger is the Disney-Pixar merger, which is known to be one of the most successful mergers of all time.

3.1.2. Disney Acquires Pixar and Marvel Entertainment

Mass media giant Disney was greeted with massive success on 2 occasions; one when it acquired animation heavyweight Pixar, and the other when it acquired Marvel Entertainment. Pixar Entertainment was acquired for 7.4 billion dollars. While Disney had already been a name to reckon with in the entertainment sector, with classics like 'The Lion King', 'Cinderella' and 'Mary Poppins against its name, it saw tremendous success with films like 'Finding Dory', 'WALL-E', 'UP' and 'Toy Story 3', many of which have grossed over a billion dollars at the box office.[7]

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[6] Prachi Juneja, 'The Whatsapp- Facebook-Instagram Merger' (*Management Study Guide,* 2022) <https://www.managementstudyguide.com/whatsapp-facebook-instagram-merger.htm> accessed 10 February 2023

[7] Diva Rai, 'The Successful Corporate Marriage (Merger) of Walt Disney and Pixar' (*iPleaders,* 8 July 2021) <https://blog.ipleaders.in/the-successful-corporate-marriage-merger-of-walt-disney-and-pixar/> accessed 10 February 2023

While Disney was able to cement its position as the topmost provider of family-friendly films by merging with the world's most innovative animation studio, Pixar was able to largely increase its production process and release 2 new films every year. These popular social media websites were initially owned by separate companies. Although the websites have continued to exist and possess their original names, they gradually, one after the other, came to be owned by one company, i.e., Facebook, owned by Mark Zuckerberg.

Soon after, Disney acquired Marvel Entertainment for 4.3 billion dollars. Since then, there has been no looking back, with Marvel rolling out films like Avengers, Black Panther, Thor: Ragnarök, and Captain Marvel, most of which ended up being amongst the highest-grossing films of all time.

3.2. Strategic Alliance

A strategic alliance is formulated when 2 or more companies agree to collaborate/cooperate, to achieve certain commercial ends. In a strategic alliance, each company retains its independent identity; no companies are dissolved or created. The idea behind such an alliance is to work together for the common benefit of all, such as increased product development, cost reduction, technology sharing, etc. The alliance between Marvel and Visa is perhaps the most appropriate, where 2 opposite poles teamed up for a common objective that befitted both.

3.2.1. Starbucks and Barnes & Noble

In today's digital world, several brick-and-mortar bookstores have closed down due to a lack of customer base. However, those who have routinely reorganized their business setup and entered strategic alliances, have survived. For instance, if one finds himself in a Barnes and Noble bookstore, he is most likely to come across a Starbucks inside, or maybe next door. On account of this partnership, Barnes and Noble has given customers more of a reason to visit its bookstores, since one can now not only browse the latest bestseller's shelf but can also have frequent coffee breaks. Moreover, this has also caused many competing bookstores to close down, since in an era where digital media sales are rising incessantly, it is indispensable that sellers dealing in printed literature reorganize their businesses in consonance with the ever-changing business environment.[8]

3.2.2. Marvel and Visa

While strategic alliances may have involved companies with completely dissimilar services, there could be nothing more bizarre than a team-up of a credit card company, and a creator of comic books and superhero movies. Visa desired to impart financial education to young minds.

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[8] Rebecca Lingley, 'Marketing Strategy and Alliances Analysis of Starbucks Corporation' [2009] Faculty Publications and Presentations <https://digitalcommons.liberty.edu/busi_fac_pubs/10?utm_source=digitalcommons.liberty.edu%2Fbusi_fac_pubs%2F10&utm_medium=PDF&utm_campaign=PDFCoverPages> accessed 10 February 2023.

To better implement its objective, Visa turned to Marvel for help. Since then, the 2 have jointly created a couple of comic books that teach money management in creative and children-specific ways.[9]

3.3. Joint venture

A joint venture, in layman's language, may seem synonymous with a strategic alliance. However, certain differences exist between them. Every business's goal is to maximize profits, and to do so, one can either go for a joint venture, or a strategic alliance, depending upon the nature and circumstances of his business. A strategic alliance, as explained above, is formed when 2 or more companies agree to share their resources, in pursuance of a certain objective. However, no new entities are created, and the concerned companies share the costs of space. On the other hand, a joint venture comes into existence when 2 or more companies agree on combining their resources, to achieve certain commercial ends. Under an incorporated joint venture, the new organization formed as a result of the integration of the companies' resources would exist as an independent legal entity; its property shall be it's own and not the property of the shareholders, and it would have a right to enter into contracts and possess property under its name.

3.3.1 Tata Global Beverages Ltd. and Starbucks

In 2012, Tata Global Beverages, the second-largest branded tea company across the globe, and Starbucks entered into a joint venture agreement in India. Through the agreement, the 2 companies created a joint organization by the name of Tata Starbucks Ltd. and decided to own one-half of the shares, each. This agreement aimed to have people enjoy the premium Starbucks experience, as well as get a taste of high-quality Indian beverages such as tea and Arabica coffee.[10] Presently, Tata Starbucks has more than 140 retail outlets across the Indian subcontinent.

3.4. Demerger

As suggested by its name, a demerger is a type of corporate restructuring strategy where a company decides to divest one or more of its business units. Such business unit(s) are broken off either to exist as independent entities or to be sold or liquidated as a divestiture. Companies usually decide to sell off their non-core brands or business units to raise capital and focus on their business's core and most profitable product lines, in times of financial difficulties. Demergers might also be undertaken in cases when the company decided to establish separate legal entities to handle separate operations, in the event of one or more of its business units underperforming and

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[9] Visa Inc, 'Visa Teams up with Marvel to Offer Financial Education through "Guardian" Comic Book' (*Pr News Wire,* 7 May 2016) <https://www.prnewswire.com/news-releases/visa-teams-up-with-marvel-to-offer-financial-education-through-guardian-comic-book-300264635.html> accessed 11 February 2023

[10] 'Starbucks Inks Joint Venture with Tata to Open Coffee Shops in India' (*Proactive Investors*, 30 January 2012) <https://www.proactiveinvestors.com/companies/news/83248/starbucks-inks-joint-venture-with-tata-to-open-coffee-shops-in-india-24201.html> accessed 10 February 2023

reaping lesser profits. This, in turn, increases the company's overall performance, since specialists are handling the separate business units, rather than generalists. The company, whose business components are transferred to the other company is referred to as the demerged company, while the company that receives them is termed as the resulting company. A demerger could take place either in the form of a spin-off, or that of a split-off.

3.4.1. Spin-off

A spin-off is said to occur when the parent company divests its business units to exist as independent companies. The parent company and the divested units exist as separate corporate entities, once the spin-off is complete. Companies usually undertake spin-offs when they feel the need to focus primarily on their core assets, or that the true potential of the business can only be achieved if the units are managed under an independent management structure.

Consider a company ABC, which handles various businesses, including cosmetics, sportswear, handbags, and shoes. ABC's sportswear section is performing well, but since the company's primary segment is cosmetics, it is not able to focus properly on the former. Thus, to improve its efficiency and maximize profits, the shareholders decided to divest the sportswear section to exist as a separate company, with an independent management team, CEO, resources, etc. In this case, the shareholders of ABC would be the same as the shareholders of the resulting company.

An important point to note here is that in a spin-off, since the parent company is not dissolved, shareholders are not allowed to give up or exchange any of the existing shares in the parent company. Instead, they are given shares in the new company on a pro-rata basis.

3.4.1.1. eBay creates spin-off PayPal

One of the most prominent recent cases of spin-off occurred when the financial company PayPal spun off from American multinational e-commerce corporation eBay. Before the spinoff, shareholders received one share of PayPal for every share of eBay they owned. However, over time, shareholders realized the potential of PayPal to exist as an independent company. In a statement, eBay explained that the foremost reason for divesting PayPal was to enable both companies to focus more effectively on their respective commerce and payment markets.[11]

3.4.2. Split-off

[11] 'EBay and PayPal Spin-Off, an Analysis - Blogs' (*Televisory*, 24 November 2017) <https://www.televisory.com/blogs/-/blogs/ebay-and-paypal-spin-off-an-analys-2> accessed 10 February 2023

A split-off is like a split-off in the sense that both involve the parent company divesting one or more of its business sectors. However, in the former, the divestiture is performed under specific structured terms. For instance, while a spin-off does not involve the giving up or exchange of the existing shares in the parent company, in a split-off, the parent company offers its shareholders the choice of either retaining their shares in it or exchanging them for shares of the divesting company. A significant factor that differentiates this method from other divestiture ones is the distribution of shares; here, shares of the new company are not distributed on a pro-rata basis.

3.4.2.1. The Viacom-Blockbuster split-off

This is one of the best-known illustrations of a split-off. Due to the rising number of cheaper DVD retailers, Video-on-demand services like Netflix, and digital recording capabilities of traditional TV set-up boxes, Blockbuster had begun feeling the heat. As a result, in 2004, Viacom split off from Blockbuster to rid itself of the underperforming division.[12]

3.4.3. Split up

A split-up occurs when the parent company breaks down into 2 or more independent companies. In contrast to the situation in a spin-off, in a split up, the parent company ceases to exist. Therefore, in this case, the shares in the old company are exchanged for shares in the new company. Shares are distributed in the same proportion as held in the original company. There are several reasons why a company may go for a split up. The company may have to split up in adherence to the mandates of the Government concerning monopolistic practices. Also, if the company has several business sectors and is unable to focus effectively on all, it may decide to break up into separate components, to better its efficacy.

3.5. Franchising

Franchising is a great way of widening the boundaries of one's business, without incurring any additional costs. This restructuring technique involves a party granting certain rights to another party, concerning its business. These rights may involve the authorization to sell one's goods or services and to exploit one's trademark and brand name. In turn, the party granted such rights (franchisee) pays a one-time fee (i.e., royalty) or commission, and possibly a share of the profits earned to the parent business (franchisor). Franchising is beneficial both for the franchisor and the franchisee. While the franchisor can help establish its goodwill in a larger number of areas, reach more customers, and build a brand name, the franchisee may incur a much lower risk than that involved in setting up a

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[12] 'Viacom and Blockbuster to Divest Using a Split-off Exchange Offer' (*Dallas Business Journal*, 18 June 2004) <https://www.bizjournals.com/dallas/stories/2004/06/14/daily43.html> accessed 11 February 2021

new business, since the parent business has already been tried and tested. Moreover, banks are also more likely to grant loans to businesses with a credible reputation than start-ups.

3.5.1. The Coca-Cola Company

The Coca-Cola Company has established a formidable reputation on account of its world-famous beverage, Coca- Cola. One of the major reasons for its rapid development and marketing success is its franchising strategy. The Company has been franchising its business to bottlers worldwide, which has in turn helped it adapt its business strategies in sync with the changing business environment. For instance, during its early days, when the company wanted to expand its business nationwide, it sought the assistance of US-based franchises, and when it desired to go beyond the nation's boundaries, it turned to international franchises.[13] Right from its birth, the Coca-Cola Company, unlike its rivals, has not focused much on market expansion by constructing its facilities nationwide. Rather, it has routinely focused on franchising its business to bottlers, which has helped it save the costs that it could have spent on constructing its facilities nationwide and internationally, and expand its market at a much faster pace.

3.5.2. McDonald's

One of the best examples of franchising is one involving the world's leading fast-food company, McDonald's. While there are currently more than 38,000 McDonald's restaurants spread across the globe, merely 6% of them are owned by the fast-food giant. This is evidence of the extent to which McDonald's has franchised its business over the years to increase its reputation and customer base.

4. Conclusion

As witnessed in various cases explained above, corporate restructuring allows a company to continue to thrive in a changing business environment. There can be various modes through which a company can realign its business operations to ensure greater profits, diversification, and larger customer bases. Reorganizing one's business and financial operations would ensure that even when all is doom; when the company is forced to pieces due to its financial woes, there remains hope that the divested pieces could function well enough for a buyer to acquire the diminished company and take it back to profitability.

[13] 'The Franchising Strategy of the Coca-Cola Company Essay' (*Free Essay*, 17 May 2016) <https://freeessays.club/the-franchising- strategy-of-the-coca-cola-company/> accessed 10 February 2023