Corporate Restructuring – Recent Experiences, Future Outlook

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In the aftermath of the financial crisis the term corporate restructuring has become synonymous with "debt restructuring", at least for a large part of the undiscerning public. But the term "corporate restructuring" is also used when group entities are restructured to achieve commercial objectives with increased efficiency without losing market share or credibility. The purpose of this article is to point out basic features of both with more focus on the latter (corporate restructuring as opposed to debt restructuring) and provide a future outlook for the same in UAE based on our recent experiences.

Debt Restructuring
Corporate restructuring to manage debt (also called corporate debt restructuring) is used when a company is having trouble making payments on its debts. It is usually undertaken in response to an extreme financial crisis. In theory, after a restructuring exercise, payments should be manageable. Generally, a corporate debt restructuring will be accompanied by cutting operating expenses, altering the firm's business portfolio by selling or acquiring assets and/or changing the firm equity ownership structure. Such restructuring can either be out of court through mutual settlement with major creditors (usual threshold is creditors owed at least 75% of the debt) or through court processes such as Chapter 11 of the U.S. Bankruptcy Code which enables debt burdened companies to approach the court with a debt restructuring scheme. In most cases under Chapter 11, schemes for restructuring debt is pre-packaged; that is, agreed with major creditors before being taken to court: creditors are taken on board and agreements entered into with the creditors before an application is filed under the bankruptcy code. The whole process can be completed in a matter of weeks. The pre-packaged bankruptcy proceeding is particularly helpful in cases where out of court settlement is not practical or easy due to complicated debt structure of the company.

Corporate Restructuring
In certain instances, servicing debt is not always the main objectiveof corporate restructuring: the objective may be to improve operational and financial performance, explore strategic opportunities or improve public market valuations. In this sense "corporate restructuring" covers all forms of legally accepted measures by which one or more corporate entities can alter corporate form to affect current relationships with third parties and even amongst shareholders of the corporate entity subject of restructuring. Broadly speaking corporate restructuring can take the form of:

- corporate expansion (merger, acquisition, joint venture);
- corporate contraction (spin-off, divestiture, carve-out (including equity carve-out), asset abandonment, liquidations, deregistration of corporate entities; and
- ownership and control (purchase of own shares and conversion to a private company (whether by a leveraged buy-out (LBO) or by other means)).

Economic realties have forced managers to reassess the need to retain extensive group structures and, if required, to replace with ones designed to efficiently serve core business objectives. In our experience another challenge in recent times to existing corporate structures has come from the business side, especially when they (existing corporate structures) impede a natural shift in business strategy called for by the need to explore new businesses opportunities.

Whatever the reasons, a corporate restructuring exercise is desirable if it achieves identified corporate needs, the bottom line always being improved efficiency and profitability of the company.
Motives behind corporate restructuring matters in which the firm has been involved recently are diverse; some are as follows:

- to close down entities that are not adding any value to the business;
- reduce operating cost by downsizing corporate group, but add activities on licenses of the reduced group entities to conduct business unaffected;
- outsource non core activities such as HR management, accounting and other back office functions to third parties or affiliates and reorganize the group entities;
- reduce intermediary costs by incorporating entities or adding relevant activities to existing corporate licenses to conduct distribution through self owned retail outlets or subsidiaries;
- reorganize group entities in the region to fall under subsidiary in UAE to avail tax free status and benefit on repatriation of dividends to foreign parent company under avoidance of double taxation treaty between UAE and the country where the foreign parent company is domiciled; and
- consolidate group companies set up in the region under holding structure set up in an off shore jurisdiction to achieve uniformity in corporate policy, better administration and manage exit strategy.

Conclusion

We envisage that the recent increase in corporate restructuring witnessed in the UAE will continue to grow as managers strive to reduce operating costs and realign existing corporate group structures to long term business strategy. In terms of holding structures we see UAE continuing as a hub for tax planning particularly for parent companies based out of Europe which is likely to experience higher taxes going forward. Finally, big corporate brands are likely to restructure their corporate presence in the UAE to facilitate direct sale to end consumer through self owned retail outlets or distribution network rather than use intermediaries.