

Legal organization simplification

ADDRESSING A BLIND SPOT



Extending organizational transformation approaches to simplifying underlying legal structures – cutting through bureaucracy and removing complexity in legal entities and branch organizations

Many industries are facing multiple disruptive factors: the Covid-19 pandemic, technology, political uncertainty, changing market dynamics or customer demand. Corporates are reacting to these changes by rethinking and streamlining their organizational and operational setup to address changing strategic objectives and introduce more agility into their businesses.

However, many corporates risk leaving considerable value on the table by failing to address and rationalize the underlying legal organizational structures. While functional teams are becoming more agile, the underlying

legacy legal structures remain unnecessarily complex and burdensome to administer. These structures can also become an obstacle to effective corporate governance and efficient internal procedures such as accounting and tax management.

While tackling this can be challenging, there are a number of criteria that will lead to the successful simplification of a legal organization:

- senior management buy in and support;
- rigorous program and stakeholder management; and
- subject matter experts across the diverse business, legal, governance, and tax functions.

It is a challenging combination; the rewards, however, can be substantial, particularly if this is done within a wider turnaround or restructuring program. The operational and organizational changes will be reflected in the legal structure, creating a more efficient and streamlined business in the long-term.

Accelerating disruptive cycles call for new organizational and operating models – yet legal structures are often neglected

Across industries corporate officers and directors are faced with numerous, accelerating disruption cycles. This has led many corporates to embrace transformation and anticipate innovation and change. Leading through disruptive cycles is becoming the new central organizational design principles as it affords businesses greater agility and efficiency in increasingly complex business conditions

Yet, in most organizational transformations, the underlying corporate legal structure is rarely in focus. These structures have grown significantly over time and have outlived their initial implementation rationale.

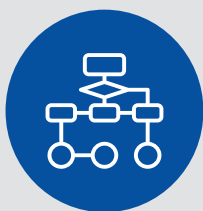
Extending the approaches for organizational and operational transformation to address the legal organization is certainly challenging – yet can turn a group transformation effort from a managerial development exercise into very tangible changes with substantial cost savings and wider benefits for the organization.



BENEFITS OF SIMPLIFYING THE LEGAL ORGANIZATIONAL STRUCTURE



Reduction of
governance
complexity



Process
streamlining



Support
footprint
optimization



Facilitation
of risk,
compliance,
controls



Improvement
of tax position



Administrative
cost savings

Transforming the legal organization into a clear and lean structure can realize benefits both for internal governance and business operations, as well as cost savings, as demonstrated below

REDUCTION OF GOVERNANCE COMPLEXITY

Reducing internal legal complexity and layers (management, committees, fiduciary mandates, accounting, register and tax obligations, etc.) requires less internal alignment and limits chiefdoms, duplication and inefficiency.

This enables a more agile and direct management approach across the entire organization. It also supports business resilience as the impact and consequences of business risk incidents are more transparent and can be addressed immediately through alignment of ownership and oversight.

PROCESS STREAMLINING

Streamlined governance and legal organization also paves the way for cleaner gatekeeper processes, such as tiered management committees. This reduces duplication and inefficiency across the organization and allows for the faster adoption of process changes and innovation.

SUPPORT FOOTPRINT OPTIMIZATION

Legal organization simplification goes hand-in-hand with operational footprint optimization. Tearing down legacy legal dividers of business operations enables footprint discussions that would otherwise often seem impossible and makes future business improvement initiatives easier to implement and increases their chances of success.

FACILITATION OF RISK, COMPLIANCE, CONTROLS

Fewer legal entities increases transparency across the organization and decreases the dilution of accountabilities. The key success factors for achieving this are effective leadership systems that promote team accountability and empowerment with a commitment to risk-management, a culture of best practice compliance, and controls that prioritize transparent communication and the regular flow of information.

IMPROVEMENT OF TAX POSITION

'Taxes' are often cited as the rationale for complex legal structures. In reality, it is seldom the case that the tax benefits outweigh the disadvantages of additional legal complexity.

In practice additional legal entities can impede the group-wide tax position, in particular the offsetting of profits and losses of different businesses. In our experience, simplification can reduce group-wide tax payments by 5 to 10% without any detriment to the corporates' in-country obligations.

ADMINISTRATIVE COST SAVINGS

Each legal entity creates continuous administrative work – corporate filings, tax and legal advisors, internal costs for administration and processes, duplication of reporting etc. With large differences across jurisdictions, we have seen annual run-rate reductions between €25,000 and €100,000 per entity or branch.

WHY ARE COMPLEX LEGAL ORGANIZATIONAL STRUCTURES OFTEN DIFFICULT TO CHANGE?

Even in the context of significant organizational and operational transformations, many corporates refrain from examining and challenging legal organizational complexity.

The undertaking is certainly not trivial and requires the collaboration of several stakeholders and experts. And, the obstacles often cited for delaying a legal organization transformation are seldom reflected in reality:

LIMITED TRANSPARENCY

The complexity of the legal organization is often not fully visible to senior management as, typically, the central performance reporting metrics focus on managerial structures. The true cost associated with complexity and, even more so, internal governance challenges are often hidden in layers of management and spread across cost centers. Identifying the case for change therefore requires explicit analysis across the organization.

COMPLEXITY OF REQUIREMENTS

Legal, regulatory, or tax requirements across jurisdictions naturally drive legal structure complexity. Yet a rigorous, in-depth review often reveals that the majority of these requirements can be addressed without additional legal organization complexity. In addition, the rationale that originally supported the creation of additional entities or branches has lapsed over time – yet it continues to be cited for the sake of consistency or even unwillingness to consider change.

DIFFICULTY TO QUANTIFY BENEFITS

While many agree intuitively that reducing legal structure complexity will reduce cost, it takes rigor to identify the relevant savings across multiple business units and functions and time to drive a program to results. Both require commitment and resolve from senior management.

TIMELINE

Legal restructuring requires numerous complex internal steps as well as significant administrative and register requirements across jurisdictions. This unavoidably takes time and can often turn into a multi-year process. To build momentum, quick wins are critical – but overall, the effort requires stamina for rigorous multi-year planning and execution.

OPERATIONAL AND FINANCIAL RISKS

Legal restructuring comes with diverse operational and financial risks that need to be carefully navigated: Balance sheet values might be forfeited, jurisdictional permission might cease, contracts might be affected, employee transfers might increase costs, or claims for compensation and tax risks might arise as part of deregistration. No doubt, the organization and external advisors will bring up numerous reasons why changes are not possible or just too difficult. It takes resolve and expertise to challenge, weigh up, and address all of these – but experience shows that much more is possible than the early expert assessment initially suggests.

CHIEFDOMS

Decentralized chiefdoms thrive on legal organization complexity and vice-versa. The position of management with its fiduciary duties, corporate responsibilities and leadership reputation can create decentralized power. This can impede the adoption of any group-wide common processes that drive efficiency, agility, speed of execution, entrepreneurialism, innovation and long-term value. Reasoning alone may often not succeed here, however adopting performance metrics that incentivize and reward a culture of clear reporting lines and the flow of information between teams can work to break down these structures. Creating interdependencies within the organization, such as common resources and stakeholders, distribution of profits and capital will also deliver results.

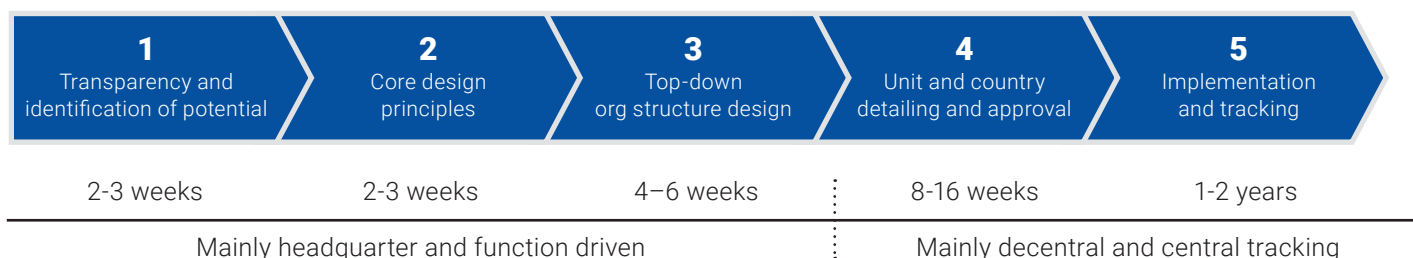


HOW TO EFFECTIVELY CHALLENGE AND RESTRUCTURE COMPLEX LEGAL ORGANIZATIONS

Despite all the challenges laid out above, effective programs can be run to radically reduce the complexity of legal organizational structures. A number of key success criteria include:

- assertive top management who drive with a clear mid- to long-term perspective and who communicate and demonstrate the importance of the program;
- senior program leadership with a business or financial background rather than legal, tax, or other functional experience. This is critical to face the change resistance typically perceived in the concerned units;
- rigorous project management, both for planning and implementation; and
- a project team that combines a sound understanding of the challenges with thorough subject matter expertise to drive and challenge legal, tax, and other counsels and obtain pragmatic and results-oriented advice.

A multi-step approach as shown in the diagram below, which starts in the corporate headquarters and swiftly devolves business management, legal and tax expertise across jurisdictions.

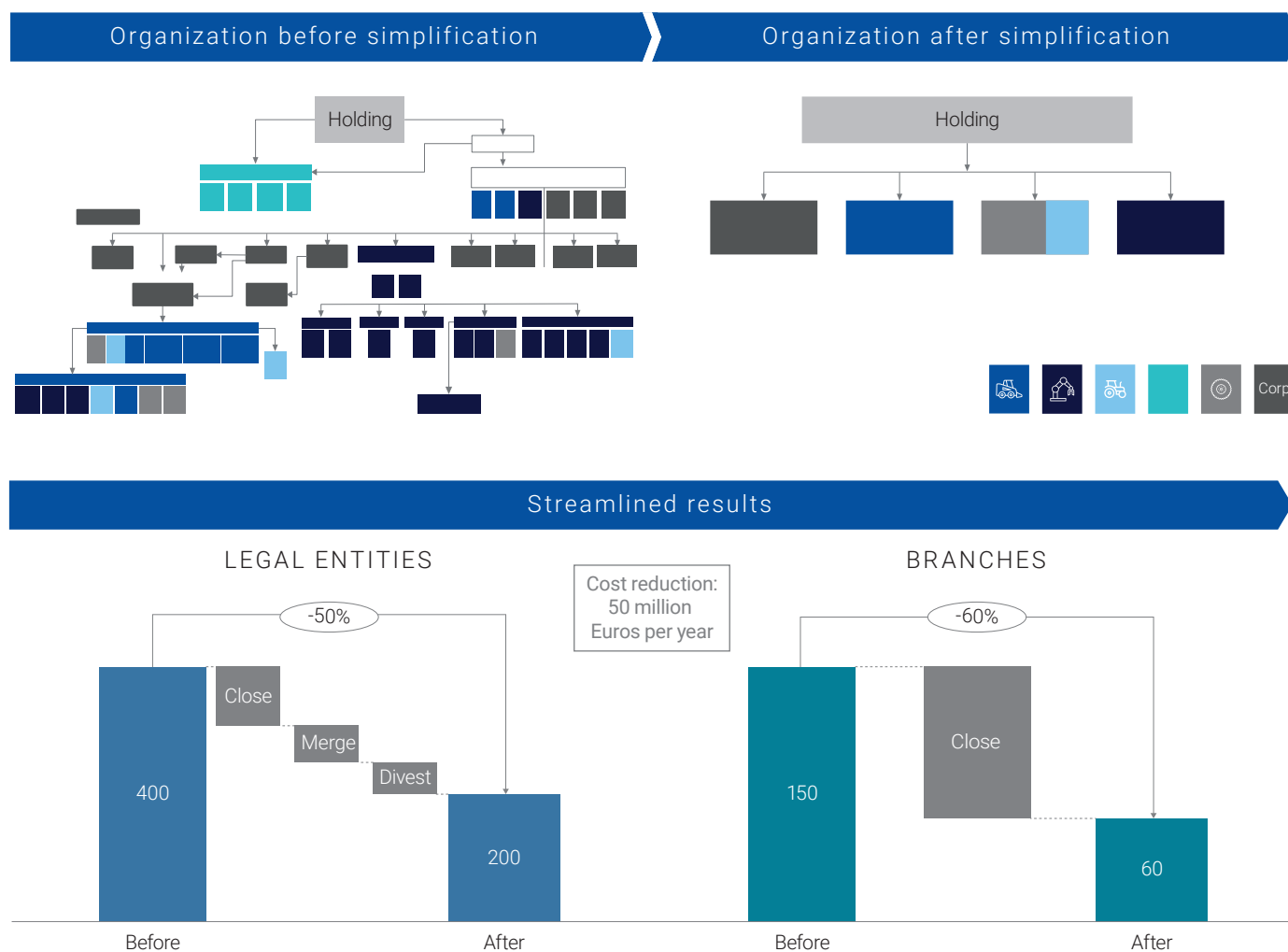


- 1 Transparency and identification of potential:** The initial step in the first two or three weeks is fully understanding the status quo of the group-wide legal organization, the underlying rationale and its relation to the management structures. This will serve to identify the potential and specific critical challenges to address upfront.
- 2 Core design principles:** The second two to three week phase fleshes out the overall ambition and establishes the core design principles, for example a 'one entity per country' principle and standards for eventual justifications for deviations. Close alignment with top stakeholders across businesses units, functions and geographies is key.
- 3 Top-down org structure design:** Phase 3 of four to six weeks involves drafting a high-level target legal organization blueprint for all geographies. Built in the headquarters, it necessarily originates in a top-down manner applying the core design principles.
- 4 Unit and country detailing and approval:** In a significantly longer phase 4 of eight to 16 weeks, the centrally developed plans will be reviewed and detailed in close collaboration with the business units or countries. The involvement of local internal or external experts, e.g. legal and tax advisors, becomes important. The phase leads to detailed restructuring plans for each unit or country approved by corporate headquarters and the relevant local leadership team.
- 5 Implementation and tracking:** This may typically take up to two years. It comprises business, finance, tax, HR and legal activities. Avoiding dilution of the agreed outcomes, rigorous central tracking is critical to ensure delivery of the program. A standing team to handle group legal structures – which should be established in any case – will typically be integrated into a legal, finance, or corporate development function. To be truly effective, and deliver the desired outcomes, this program requires a business leader and cross-functional team to run and implement a group-wide change program.

CASE STUDY:

Simplifying the group-wide legal organization for a globally active technology corporate

This organization was in the process of transforming its management organization from a complex matrix organization into a lean, customer focused and decentralized unit driven organization. The client also set out to restructure the legal organization into a clear and lean target state per country.



Impact: The restructuring plan aimed to reduce the group's existing 400+ legal entities and 150 branches by more than 50%. This will result in cost reductions of approximately €50 million annually, as well as a significant simplification of governance structures.



CONCLUSION

Restructuring the legacy legal organization of a large international business into a lean target structure is an ambitious endeavor. The complexity of individual situations across jurisdictions including tax, legal, business interests, finance and reputation, is immense. Even more challenging can be the numerous and very diverse stakeholders, central and devolved, many of whom may not be supportive, choosing instead to focus on potential risks and obstacles to change.

Yet, there are clear rewards for undertaking this challenge. Cost savings are a significant benefit. In addition, there are critical improvements to organizational hygiene and group-wide effective governance as greater focus is placed on environmental, social and governance (ESG) criteria by investors.

Companies would be wise to supplement their ongoing organizational transformations with a rigorously designed program that also addresses their governance systems and legal structures. Top management needs to set clear ambitions, mandate an experienced and engaged project team, and ensure buy-in for the process – even if challenges arise and implementation pay-off may take several years.

Our experience shows that a legal organization simplification program can deliver great value if set up and managed effectively. Where the right momentum is established and stakeholders are aligned, seemingly insurmountable challenges become manageable – and impact may materialize faster and more widely than expected.

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ABOUT US

For nearly forty years, AlixPartners has helped businesses around the world respond quickly and decisively to their most critical challenges – circumstances as diverse as urgent performance improvement, accelerated transformation, complex restructuring and risk mitigation.

These are the moments when everything is on the line – a sudden shift in the market, an unexpected performance decline, a time-sensitive deal, a fork-in-the-road decision. But it's not what we do that makes a difference, it's how we do it.

Tackling situations when time is of the essence is part of our DNA – so we adopt an action-oriented approach at all times. We work in small, highly qualified teams with specific industry and functional expertise, and we operate at pace, moving quickly from analysis to implementation. We stand shoulder to shoulder with our clients until the job is done, and only measure our success in terms of the results we deliver.

Our approach enables us to help our clients confront and overcome truly future-defining challenges. We partner with you to make the right decisions and take the right actions. And we are right by your side. When it really matters.

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