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Revolutionizing Legal Entity Rationalization: The Power of Early IT Integration for Faster, Cost-Effective Restructuring

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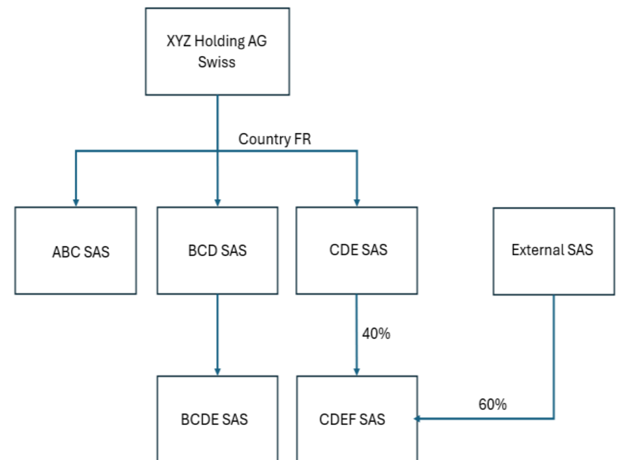
***Abstract*— Legal Entity Simplification (LES) or Rationalization (LER) is an increasingly important strategy for large organizations seeking to reduce costs, improve operational efficiency, and leverage tax benefits by restructuring their legal entities. Traditionally, IT systems such as Enterprise Resource Planning (ERP) are introduced late in the LES process, which often leads to higher costs, delays, and integration challenges. This research paper presents a new methodology for incorporating IT early in the LES process, highlighting the profits of early IT involvement in identifying potential technical limitations, aligning system requirements, and streamlining the overall project timeline. The proposed approach is illustrated through a successful case study of a global agrochemical company, which implemented LES in over 15 countries using the revised methodology. By integrating IT from the beginning, the company achieved faster, more cost-effective results, minimizing disruption and ensuring the timely completion of the restructuring process. This paper demonstrates that early IT integration can significantly improve the LES process, reducing costs, minimizing risks, and enhancing overall project efficiency.**

I. INTRODUCTION

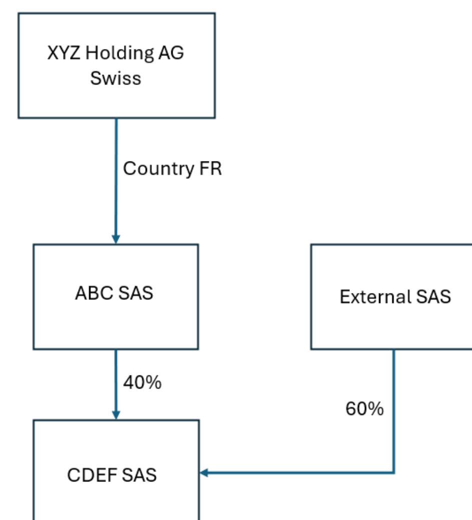
Legal Entity Simplification (LES) or Rationalization (LER) is a strategy that large companies use to improve their efficiency, reduce operational costs, and gain tax benefits by reorganizing their legal structures. These strategies often come into play after mergers and acquisitions (M&A), where the newly acquired companies continue to operate as independent entities. As time goes on, managing multiple separate entities becomes increasingly complex and inefficient, creating challenges in areas such as compliance, reporting, and resource allocation. To address these inefficiencies, organizations choose to restructure their legal entities (LE), consolidating them into fewer, more streamlined entities. This process helps reduce administrative costs, improve overall operations, and create a more agile and cost-effective business model.

A Legal Entity rationalization can be understood from the below example:
XYZ Holding AG is a Swiss Entity and has operations in France. It has 5 legal entities in France and below is the holding/subsidiary relationship among the LE:



LES/LER desire models:
The below are the two simplified legal entity structures between XYZ and its subsidiaries.

Option 1: A desired simplified structure, All LEs are fully merged into 1 existing LE. Legal Entity BCD SAS, BCDE SAS, and CDE SAS are fully merged operationally into ABC SAS.



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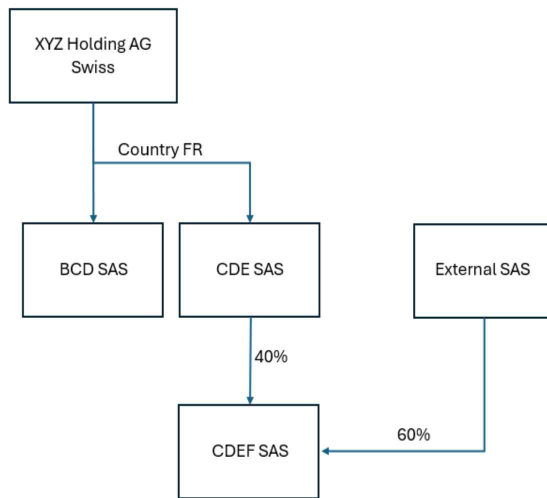
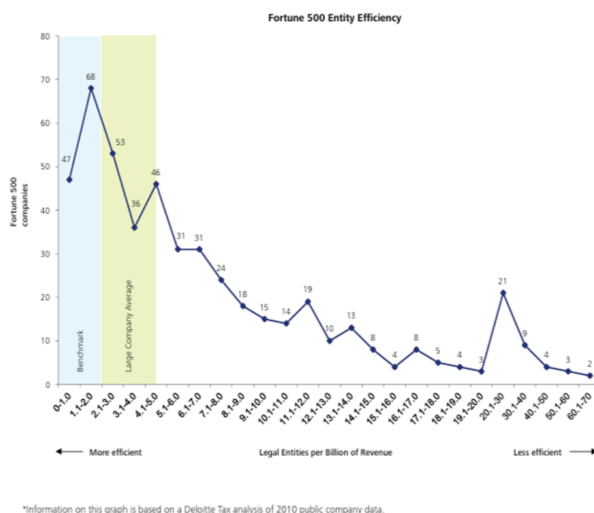
Option 2**:** A relatively simplified structure by reducing the number of LEs. Legal Entity ABC SAS and BCDE SAS are fully merged operationally into BCD SAS.



II. LITERATURE REVIEW:

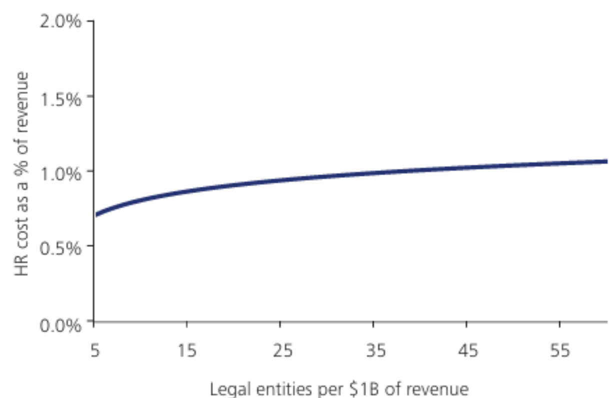
In 2010, Deloitte conducted a study on Fortune 500 companies to analyze the number of legal entities required to generate one billion dollars in revenue. The results align with expectations. Of the Fortune 500 companies, 115 have one or two legal entities (LEs) per billion-dollar revenue, making them the most efficient organizations. These companies serve as the benchmark in the report. Additionally, 250 companies from the Fortune 500 have five or fewer LEs to generate one billion dollars in revenue.



Another study by Deloitte examines the percentage of revenue spent on Finance and HR cost centers per billion dollars of revenue, in relation to the number of legal entities. The findings show that both Finance and HR expense ratios rise as the number of legal entities increases.

In the case of finance cost, companies with five or fewer legal entities spend about 1.1% of their revenue per billion per year on these functions, while this ratio increases to 1.7% when the number of legal entities exceeds 50. In dollar terms, this represents an increase of approximately USD 6 million per year per billion dollars in revenue spent on Finance alone when the number of legal entities grows from 5 to 50.

In the case of HR cost, companies spend approximately 0.7% of their revenue per billion dollars if they have 5 or fewer legal entities, but this increases to 1.1% when the number of legal entities exceeds 50. In dollar terms, this results in an increase of USD 5 million per year per billion dollars in revenue spent on Finance alone as the number of legal entities rises from 5 to 50.



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It is expected a similar trend for other administrative cost centers as well. The ideal number of LEs depends on various factors, such as the number of countries in which a company operates, future strategy or product lines, etc. However, the data clearly suggests that maintaining an optimal number of LEs is a more effective approach.

III. LES/LER APPROACHES:

The approaches used by accounting firms to assess and simplify an organization's legal structure are below:

Dormant First: This approach focuses on eliminating dormant or inactive entities, allowing for a swift transition. It is a simplified form of LES that requires minimal effort and few changes to existing business operations. In some cases, organizations adopt this strategy by having the acquiring LE gradually merge the operations of the acquired entity into their existing structure. However, this method typically does not result in significant cost savings.

Outside In: This is the most commonly used approach. It involves reviewing the entire organizational structure and simplifying it to create a more streamlined framework. Some entities remain intact, while others are merged operationally to optimize the organization’s structure.

Straw Method: The newest approach, the Straw Method, disregards existing entities and creates an entirely new organizational structure. New entities are established, and all existing entities are operationally merged into this fresh framework.

IV. KEY FACTORS IN RESTRUCTURING.

There are various factors impact the organization's Legal entity restructuring. The most common evaluation criteria are listed below:

1. Human Capital Management:
Merging employees across entities involves addressing various key aspects such as employee contracts, retirement benefits, and contractual terms. It is important to evaluate how layoffs or workforce restructuring will be handled, as well as the need for new skill development and training. Additionally, salary realignments may be necessary to ensure consistency across the newly merged organization. All these factors require careful planning to ensure a smooth transition for the workforce.

2. Tax Planning/Compliance:
Tax planning is a crucial consideration during the merger of entities. One of the primary concerns is whether any special tax incentives associated with the existing LE will be lost. Additionally, it is important to determine if tax losses can be carried over to the new LE, and whether combining multiple LEs could push the new entity into a higher tax bracket. A thorough analysis of these tax implications is essential to avoid potential financial setbacks.

3. Operational Viability:
Evaluating the operational viability of each entity involved in the merger is critical. This includes assessing market share, the goodwill of each LE, and the potential impact of the merger on brand value. Retaining brand integrity and aligning sales representative training and bonuses are key considerations. Additionally, determining whether the business models and products of the entities are similar and whether amendments to the organization’s Articles of Association (AOA) are needed, must be carefully reviewed.

4. Large vs. Small LE:
When merging subsidiaries, it’s important to consider the relative size and ranking of each LE. Typically, smaller entities are merged with larger ones to improve operational efficiency. However, the similarity of business models and operations also plays a crucial role in determining how best to structure the merger. The size and compatibility of the businesses involved can significantly influence the overall success of the integration process.

5. Patent/Intellectual Property:
The handling of patents and intellectual property (IP) is another critical consideration during the merger. It must be determined whether these assets are transferable to the new LE without issues. Additionally, the loss of patents or IP could negatively impact the company’s competitive advantage and overall expertise. Therefore, the legal and operational implications of transferring or losing these assets must be thoroughly assessed.

6. Existing Vendor Contracts:
Merging existing vendor contracts is a complex process that requires careful attention to detail. It is important to evaluate whether these contracts are transferable without renegotiation and whether the merger could lead to bulk purchase incentives or other advantages. Additionally, the number and value of vendor contracts across the LEs should be compared to identify opportunities for cost savings or potential challenges.

7. Existing Customer Contracts:
Merging existing customer contracts requires a detailed review of their terms and conditions. The transferability of these contracts without renegotiation must be established, along with any potential impact on existing agreements, particularly government contracts. Understanding the contractual obligations and ensuring that customer relationships are maintained will be key to the success of the merger.

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V. IMPLEMENTATION METHODOLOGY

The success of any project is measured by how efficiently it is implemented. Legal Entity Rationalization (LER) projects are particularly sensitive, with wide-ranging implications for the entire organization. A single wrong action can be very costly. Timely involvement of all necessary stakeholders is also crucial for the success of LER projects. Below are the traditional and revised implementation methodology for LER projects.

A. Traditional Methodology

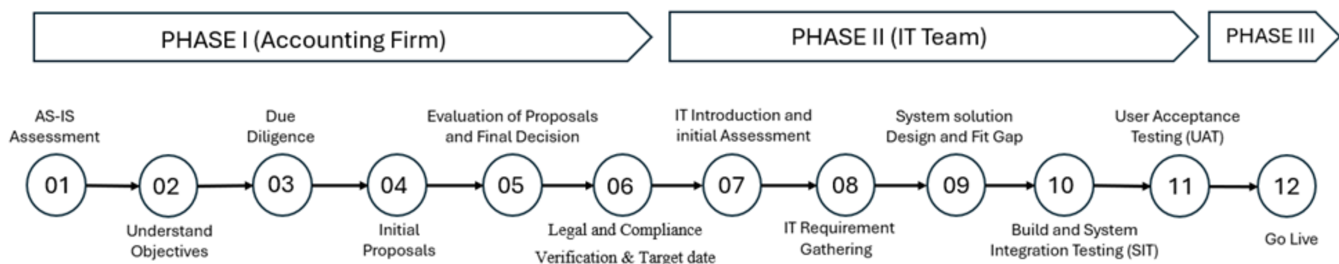
The traditional approach to Legal Entity Simplification is a three-phase process from start to end.

- Phase I focuses exclusively on the Accounting firm, aiming to understand, design, and finalize the restructuring. Steps 1 to 6 below are part of Phase I.
- Phase II is dedicated to the IT team, who will build the system based on the finalized design. Steps 7 to 11 below are part of Phase II.
- Phase III marks the go-live phase, where IT will manage the cutover and prepare the system for the new legal entity structure, while the Accounting firm handles the legal and operational aspects. Below step 12 is part of Phase III.
- Phases I and II are separate, with minimal interaction between the IT team and the Accounting firm. Below is a summary of the current methodology:

4. Initial Proposals: Develop initial restructuring proposals, typically providing multiple options in complex cases. The proposals should align with organizational objectives and avoid negative business impacts. All advantages and disadvantages of each proposal must be clearly outlined.
5. Evaluation of Proposals and Final Decision: Hold a series of meetings, workshops, and consultations with business leaders and stakeholders to review each proposal. Based on thorough analysis, make a final decision on the restructuring plan.
6. Legal and Compliance Verification & Target Date: Final verification of the selected solution against legal frameworks and regulatory requirements to ensure full compliance. This step also includes setting a target implementation date.

Phase II: IT is included in this phase and below steps are covered under this phase:

7. IT Introduction and Initial Assessment: Introduce the IT team and present the final solution. Conduct an initial assessment of the IT feasibility of the restructuring, leading to the development of a project scope and a detailed project plan.



Phase I: Below steps are covered under this phase:

1. AS-IS Assessment: Evaluate the existing legal entity structure to identify inefficiencies, and gather key data such as tax information, customer and vendor contracts, intellectual property (IP), trade Patents (TP), human resources, and operational efficiencies.
2. Understand LES Objectives: Clarify the organization's goals for legal entity simplification (LES), whether it's to reduce costs, streamline operations, or improve compliance. Assess the budgetary scope and determine the appropriate LES approach (e.g., Dormant First, Outside-In, or Straw).
3. Due Diligence: Identify potential challenges, including operational viability, human resource issues, customer and vendor contracts, IP/patents rights, and legal and tax implications. This critical assessment will shape the restructuring process.

8. IT Requirement Gathering: Collect detailed technical requirements through business discussions and workshops. Assess the impact of the new solution on the system, particularly focusing on data migration and high-level system requirements.
9. System Solution Design and Fit-Gap Analysis: Design the system solution based on the gathered requirements and define the data migration strategy. Conduct a fit-gap analysis to identify and address system solution gaps, including preparing a cutover plan.
10. Build and System Integration Testing (SIT): Develop the system and test it to ensure it functions as expected. Establish a clear migration strategy for legacy data, conduct full system integration testing, and validate the system's functionality, includingtesting data migration Any bugs should be reported and addressed..

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11. User Acceptance Testing (UAT): Users test the system to confirm it meets expectations. Any issues identified must be resolved before migrating to production.

Phase III: Go Live:

12. Go Live: Careful execution of this step is crucial, as it involves implementing numerous practical aspects of the project, including operational and legal changes. This ensures the smooth migration of contracts, assets, and employees to the new entity structure. Additionally, the organization must ensure that all legal labels are updated and that all relevant parties—such as customers, vendors, government bodies, and investors—are properly informed and communicated with.

Challenges with the Existing Approach

While the above process outlines the necessary steps for LES, it also presents several challenges, particularly when IT is involved too late:

1. Late Entry (Feasibility Study): Introducing IT late in the process limits its ability to identify technical limitations or integration issues early on. This can delay the project, increase complexity, and create potential failures.
2. Duplicate Effort: When IT joins the project later, tasks such as workshops, planning, and contract management may need to be revisited, leading to wasted effort and increased costs.
3. Higher Costs: Late IT involvement often results in higher rework costs, additional resources, and system modifications, which could have been avoided by involving IT from the start.
4. Risk of Failure: If IT is not fully integrated early on, integration challenges or system compatibility issues may jeopardize the entire project, causing delays, operational disruption, or legal non-compliance.

B. A Revised Methodology: Early IT Integration

To overcome these challenges, a new approach is proposed where IT is integrated into the LES process from the beginning. Below are the steps of the revised methodology:

- Phase I is dedicated solely to the accounting firm, focusing on understanding the current state (AS-IS), setting objectives, and completing due diligence. Steps 1 to 3 below fall under Phase I.
- Phase II is a shared responsibility. The accounting firm is in charge of the initial proposal, while the IT firm is responsible for conducting a feasibility study of the proposals. Both teams, alongside business and leadership, evaluate the proposals, select the final option, and set a target date. Steps 4 to 6 below are part of Phase II.
- Phase III is dedicated entirely to the IT team, who will design and build the system based on the finalized design. Below steps 7 to 9 belong to Phase III.
- Phase IV is the go-live phase, where the IT team will complete the cutover and prepare the system for the new legal entity structure, while the accounting firm will manage the legal and operational aspects of the go-live. Step 10 below is part of Phase IV.

Phase I and Phase III are mutually exclusive, with minimal interaction between the IT team and the accounting firm. However, Phases II and IV involve joint execution by both teams.

Phase I: Below steps are covered under this phase:

1. AS-IS Assessment: Evaluate the existing legal entity structure to identify inefficiencies, and gather key data such as tax information, customer and vendor contracts, intellectual property (IP), trade Patents (TP), human resources, and operational efficiencies.
2. Understand LES Objectives: Clarify the organization’s goals for legal entity simplification (LES), whether it’s to reduce costs, streamline operations, or improve compliance. Assess the budgetary scope and determine the appropriate LES approach (e.g., Dormant First, Outside-In, or Straw).
3. Due Diligence: Identify potential challenges, including operational viability, human resource issues, customer and vendor contracts, IP/patents rights, and legal and tax implications. This critical assessment will shape the restructuring process.

Phase II: IT is also introduced here in the evaluation:

4. Initial Proposals: Develop initial restructuring proposals, typically providing multiple options in complex cases. At the same time, IT is introduced to do a first-hand feasibility study of the solutions. Any proposals that do not comply with the IT feasibility study or are too complex for IT should be discounted at the start. The final proposal solutions should align with organizational objectives and avoid negative business impacts. All advantages and disadvantages of each proposal must be clearly outlined.
5. Evaluation of Proposals, Requirement Gathering, and Final Decision: A series of meetings, workshops, and consultations with business leaders, IT leaders, and stakeholders are held to review each proposal. Based on thorough analysis, make a final decision on the restructuring plan. IT team will collect detailed technical requirements and assess the high-level impact of the new solution on the system, particularly focusing on data migration and high-level system requirements.
6. Final verification & Target Date: Final verification of the selected solution against legal frameworks and regulatory requirements to ensure full compliance. IT also defines the scope and change management. This step also includes setting a target implementation date.
7. Build and System Integration Testing (SIT): Develop the system and test it to ensure it functions as expected. Establish a clear migration strategy for legacy data, conduct

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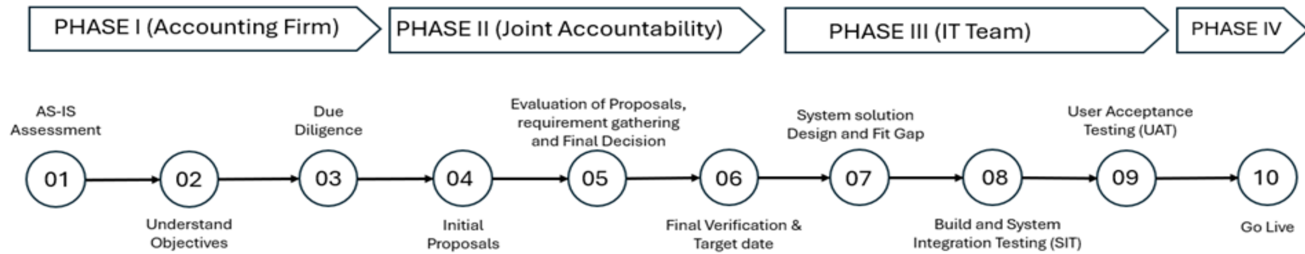
full system integration testing, and validate the system's functionality, including testing data migration. Any bugs should be reported and addressed.



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Phase IV: Go Live

9. Go Live: Careful execution of this step is crucial, as it involves implementing numerous practical aspects of the project, including operational and legal changes. This ensures the smooth migration of contracts, assets, and employees to the new entity structure. Additionally, the organization must ensure that all legal labels are updated and that all relevant parties—such as customers, vendors, government bodies, and investors—are properly informed and communicated with.

Benefits of the New Methodology

The new methodology offers significant advantages over the traditional approach:

1. Early IT Involvement: Involving IT early allows for better identification of potential challenges, ensuring technical feasibility before final decisions are made.
2. Elimination of Redundancies: Early collaboration between business and IT ensures alignment, eliminating unnecessary work and saving time and cost.
3. Proactive Risk Management: Addressing IT challenges early reduces the risk of technical issues and ensures smooth project execution.
4. Reduced Timeline: By integrating IT early, the timeline for LES implementation is shortened, leading to faster realization of benefits.
5. Cost Savings: Early IT involvement reduces the need for last-minute fixes and minimizes costly errors, thereby reducing overall restructuring costs.
6. Reduced Risk of Missing Critical Dates: Early coordination between legal, IT, and business teams ensures the restructuring can be completed by the agreed-upon go-live date, which is crucial for legal and commercial reasons.

VI. CASE STUDY: A LEADING AGROCHEMICAL

One notable application of this new methodology was seen at a leading global agrochemical company, which successfully implemented LES across more than 15 countries. By integrating IT early in the process, the Organization has reduced both time and costs while ensuring smooth, on-time transitions. According to estimates, the adoption of this methodology has saved an average of one month of time per LES project. Each LES project typically requires at least 3 to **5** IT resources. Assuming an average hourly rate of USD 100, the savings range between approximately USD 1.2 million and USD 2 million per LES program. If the organization needs to perform LES five times over its lifetime, the total savings could amount to between USD 6 million and USD 10 million. This methodology has since been adopted for additional LES projects across various regions, providing a scalable and effective model for large organizations undergoing legal entity simplification.

VII. CONCLUSION

Legal Entity Simplification is a vital strategy for organizations seeking to optimize their operations and reduce costs. Integrating IT from the beginning of the restructuring process allows businesses to avoid common pitfalls, including delays, increased costs, and missed deadlines. By adopting an early IT involvement approach, companies can streamline their LES processes, ensuring that restructuring efforts are executed efficiently, cost-effectively, and with minimal risk.

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