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# Rescuing companies before it is too late

*The longevity of companies is in danger today. It is as much the responsibility of the State as of the stakeholders to prevent their premature death*

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People invented companies in search of immortality; the companies would live and carry on their legacy. Kongo Gumi, a Japanese company engaged in the construction of temples, lived 1,429 years. There are a few 1,000-year-old companies still around. They are rare, surviving gems of a bygone era. The average life of an S&P 500 company has declined from 90 in 1935 to 18 years in 2016, according to a Mckinsey & Co report. Recent studies indicate that the average life of a publicly-traded company, considering acquisitions, mergers, and bankruptcy, is about 10 years. Clearly, the longevity of companies is in danger today.

Companies are modern engines of growth. As Colin Mayer describes, they house, feed, clothe and employ us. They hold the hope of prosperity for posterity. They often have organisational capital over and above their liquidation values. The closure of a company destroys hope and organisational capital. It takes years of effort to bring up a company, which can replace an existing one. Premature death of companies can destabilise the economy.

The life of a company has three enemies. First is the enemy within. A company is an amalgam of many stakeholders. Each stakeholder has a unique objective function, with a distinct set of rights, interests, and the level of engagement with the company. The interests of one stakeholder may conflict with those of another and/or of the company. Stakeholders may work at cross-purposes, and even against the interest of the company. Shareholders' drive to maximise their upside while enjoying limited liability may expose the company to unlimited liabilities. Examples, the Bhopal gas tragedy and the Satyam fiasco. Many shareholders hold shares for a fraction of a second, with little interest in the life of the company. This begs the question: Whose company is it anyway?

The State has prescribed certain institutional norms — independent directors, key managerial personnel, regulation of related-party transactions, protection of minority interest, financial and secretarial audit, timely and accurate disclosures about material matters, taxes and subsidies, corporate social responsibility, collectively referred to as corporate governance — to safeguard the lives of companies. These balance the interests of stakeholders and subordinate their interests to those of the company. The immediate shareholders must go beyond the minimum corporate governance norms to ward off any danger to the life of a company.

The second and the most fatal enemy is competition. It is the State policy to stimulate competition and innovation, and eliminate anti-competitive conduct for higher growth. A company, however, loses life when it fails to compete with its peers in the industry for reasons such as poor organisation, inefficient management, and malfeasance, among others. It also loses life when its business becomes unviable for reasons such as innovation, change in policy, change in social taste, or even black swan events like Covid-19. Creative destruction often destroys more companies than it creates! Strategies of resilience, adaptation, research and development, and the like, minimise the threat to life. It is left entirely to the immediate stakeholders to build muscle of the company to withstand the onslaught of competition and innovation.

The State, however, provides an insolvency resolution process to rescue a company. It has conferred extraordinary powers on creditors of a company: (a) they can take or cause a haircut of any amount to any or all stakeholders in order to rescue a company; (b) they seek the best resolution plan from the market, unlike earlier mechanisms that allowed them to find a resolution only from existing promoters; and (c) the resolution plan can provide for several measures that may rescue the company. The resolution plan may entail a change of management, technology, or product portfolio; acquisition or disposal of assets, businesses, or undertakings; restructuring of organisation, business model. Yet many companies may be beyond repair, which have to be closed. It is for the shareholders to have strategies to prevent stress in the company and for the creditors to rescue it in time.

The third enemy is unfair battles in the marketplace. For example, a company that does not have the financial muscle to sell its product below cost, cannot survive in a market where a dominant player resorts to unfair pricing. The competition law prohibits predatory pricing. Similarly, a company cannot survive if its cost of capital is high compared to another company that manipulates the market for its securities. Securities laws regulate the capital market to prevent any kind of manipulation.

A company that dutifully pays corporate tax cannot survive if another company in the same business dodges taxes. Federal taxes are often bigger than the profit-after-tax margin. If one cheats on goods and services tax, mining royalties, or income tax, it completely alters the competitive landscape, making it difficult for honest companies to survive. The rule of law is the antidote against these enemies. The State must ensure the rule of law and level the playing field to shield companies from such unfair battles. Everyone, including the State, must pay dues of vendors in time. The State must also ensure contract enforcement that brings certainty to business processes and outcomes.

The raison d'être of a company is that it must generate value and share the same among stakeholders, forever. It can do so only if it lives.

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