HOW TO SPLIT A COMPANY OR GROUP OF COMPANIES – THE PROCESS OF DEMERGER

There can be various reasons to split up a company, or a group of companies, including separating businesses in different sectors, preparing for a sale, borrowing/investing issues, where relationships between shareholders have broken down or simply, as a result of estate planning.

What is a demerger?

A demerger is a transaction whereby a business carried on by a company or shares in a company within a group is taken out of that group and run under separate management but with all, or some of the same shareholders as previously.

Why carry out a demerger?

There are many reasons why a demerger may be attractive. These include:

- **unlocking shareholder value,** e.g. where a profitable business is being undervalued by its association with another less profitable business
- **focusing management** on distinct parts of a group's business
- **ring-fencing liabilities or risks** attaching to a particular business
- effecting the demerger as a **precursor to a disposal of a business**
- **separating businesses which operate in different sectors** (giving a clearer market profile for both investors and analysts)
- **taking advantage of tax benefits,** or
- **raising finance or capital**

Any reason or motivation for carrying out a demerger must be commercial in order to satisfy the conditions for the available tax reliefs, most typically that the demerger does not form part of a scheme or arrangement of which the main purpose, or one of the main purposes, is avoidance of liability to corporation tax, capital gains tax or income tax.

Types of demerger

The main ways of effecting a demerger include:

- **Statutory demerger:** the parent company declaring a dividend in specie of the business or shares of the subsidiary being demerged
- **Liquidation demerger**: the division of the assets and businesses of the parent company in an Insolvency (Northern Ireland) Order 1989 demerger
- **Capital reduction demerger:** a reduction of share capital

Reasons for choosing a particular demerger structure

When deciding which demerger structure to choose, a company will consider a variety of tax, legal and commercial considerations, including the following:

- What is being demerged
- The shareholders' intentions and in particular, who is to own what in the end
- How the company's balance sheet is structured, and more specifically the availability of distributable reserves
- Achieving the most advantageous tax treatment both for the companies involved and their respective shareholders – to this end, advance tax clearances may need to be obtained to ensure that the demerger will be carried out in a tax-efficient manner
- Calculating the market and book values of the company being demerged
- Due diligence, shareholder and other third-party approvals, employee transfers, pensions and transitional arrangements.

Implementing a demerger inevitably takes time and careful planning.

Our tax and legal team at CavanaghKelly can provide the advice and assistance required to effect the demerger objectives.

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