Wojciech Downar
Departament of Organisation and Management
wojciech.downar@wzieu.pl

Małgorzata Rochoń
Departament of Enterprises' Economics
malgorzata.rochon@wzieu.pl

Univeristy of Szczecin
8, Cukrowa Street, 71-004 Szczecin, Poland

STAKEHOLDER APPROACH IN THE RESTRUCTURING DECISIONS

A permanent change of the environment and rapid increase in competition that often completely changes the rules for the functioning of enterprises on the market expose any economic activity to a risk and thus threatens a stabile functioning of an enterprise.

Economic deterioration and financial problems encountered may eventually threaten the further existence of a company and its capacity to meet liabilities towards creditors. This inevitably leads to a bankruptcy. An alternative to bankruptcy is a financial restructuring. The financial restructuring is a process of separating corporate finance, which is based on a fundamental change/improvement of the capital structure aimed at increasing the value of a company for creditors and/or shareholders, and improving relations with stakeholders. In other words, the financial restructuring is designed to restore liquidity and solvency in a company. The Act of 28 February 2003 on Bankruptcy and Rehabilitation Law (Polish Journal of Laws No 60, item 535) became effective on 1 October 2003. The new act provided for modified bankruptcy and rehabilitation proceedings. The new rehabilitation proceedings gives another possibility for the restructuring of a company. The goal of the proceedings is to make an arrangement between an entrepreneur and his creditors, which is a precondition of restoring a longer-term possibility for the former to compete on the market. The arrangement can be implemented if it seems obvious, after a reasonable assessment of the economic situation, that soon the company may become insolvent.

However, the entrepreneur may restructure the company according to a rehabilitation plan and make an arrangement with creditors for restructuring his liabilities. The implementation of this financial and legal arrangement depends on the status of a given company, knowledge of law and finance among the parties involved, and the capacity to make rational decisions among creditors who often perceive attempts to save a company as an activity against their own interests. The complexity of solutions applied during restructuring depends on expectations of the parties involved. On the one hand, we have debtors for whom deferred payments, reduction of debt or conversion of debt provide for restoring solvency and continuing business activity that will eventually enable them to service the debt, and on the other, we have impatient creditors for whom the lack of debt servicing translates into the worsening of their financial situation and a threat to their further functioning. Therefore, the selection of solutions for restructuring of the debtor depends on the tendency among creditors to increase guarantees and rights they are entitled to and their readiness to take a more flexible approach to debt recovery. The problem does not apply solely to creditors but rather to a larger group of organizations involved in the restructuring process. Of course, the specific character of a company determines which organizations are crucial for a successful restructuring process. These groups are described by the term stakeholders.

Defining the stakeholders is in practice very difficult, especially that the term itself lacks a clear definition. A classical definition has been formulated by R.E. Freeman: the term stakeholders shall be understood as any group who can affect or is affected by the achievement of the organization's objectives[1]. According to this definition the group of stakeholders may include many different organizations. In practical terms, stakeholders in a company include in fact only several major organizations. In the process of restructuring stakeholders that appear most frequently are, among others, the Executive Board, employees, Trade Unions, creditors, including banks and suppliers, clients, competitors and the local community. The mutual relationship between a restructured company and its stakeholders is built at the level of the strategic process of establishing goals. In general, the restructuring starts with the determining of a vision and a strategic concept for the functioning of a company. A further development of the concept involves elaborating implementation plans (e.g. revised investment, financial, and sales plans, etc.), and than the implementation of the concept, its monitoring and evaluation. None of the activities – from establishing goals to evaluating their implementation – cannot be carried out without the involvement of stakeholders. Goals are usually established together with key stakeholders (banks, other creditors, key accounts, employees, etc.). The implementation of the restructuring program involves mainly internal stakeholders (Board, employees, Trade Unions), whereas monitoring and evaluation of the program involves both internal and external stakeholders. Of course, a stakeholder may have a negative impact on the goals established. For example employees may object the program of reducing the employment, creditors may request debt to be paid, and suppliers may demand higher prices.

Ch.Hill and T.M.Jones have dealt with another important aspect of stakeholders whom they defined as constituents who have a legitimate claim on the firm[2]. Claims refer not only to their legal sense (e.g. statutory participation in decision making), but also (or perhaps first and foremost) their economic sense. During restructuring, many stakeholders invest the capital of an organization (e.g. creditors provide additional funds, employees provide labor and knowledge, etc.). Thus, each stakeholder becomes in a way an investor who, sooner or later, expects a return on the investment and a right to a residual value proportionally (or not) to their contribution. Each stakeholder runs a risk of their investment into a company. The risk may also reflect the relationship between a stakeholder and a company. The stakeholders discussed are presented in Figure 1.

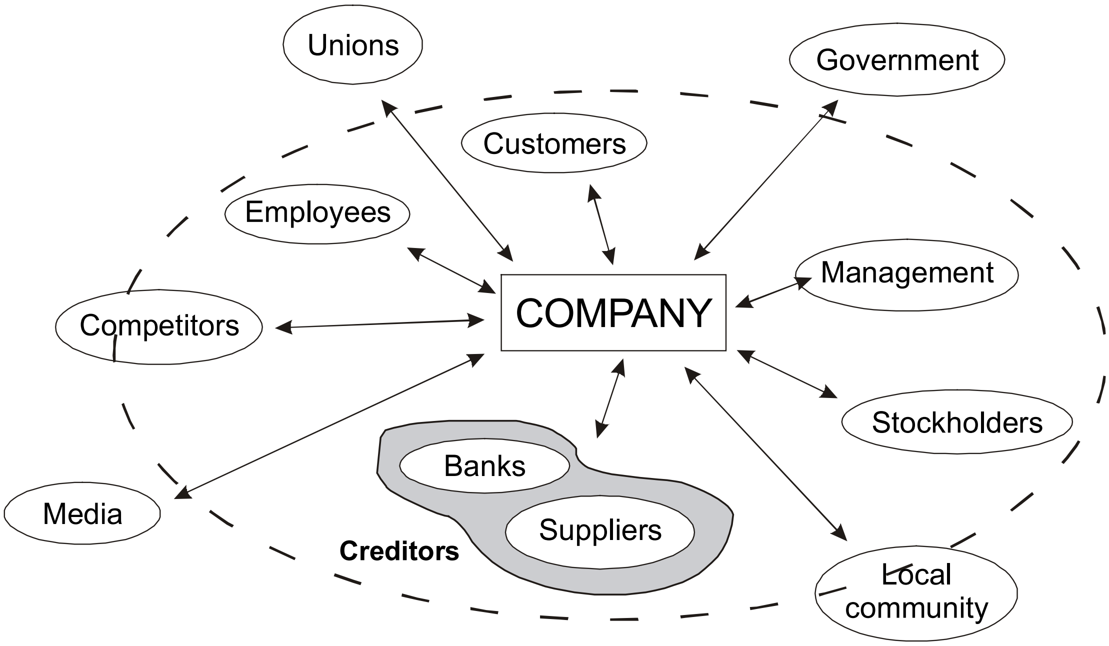
A basic issue in the process of financial restructuring is to restore trust among stakeholders - who lost it because of insolvency and related to it untimely payment of liabilities by the company – and reaching consensus with the stakeholders concerning often divergent interests under a single restructuring program. A given company may have various relations with its stakeholders, who may disagree with the concept of a proportional distribution of loss. The success of restructuring depends to a large extent on a proper communication as well as regular and precise information provided to stakeholders on the current status, results and possible progress in the restructuring of the company. At the very outset, stakeholders should be aware of the scale of problems faced by the company and should be prepared to provide the best support possible. A crucial and at the same time the most difficult issue is to define details of such a support with the stakeholders. This translates into a detailed plan for restructuring of the company, including its finance. It is difficult, since it requires from stakeholders a continuous financial involvement with the company under restructuring, and at the same time refraining from collecting the debt. Therefore, it is so important that each restructuring activity should be in line with the most efficient solutions from the point of view of stakeholders.

---

[1] R.E. Freeman, Strategic management: A stakeholder approach. Boston: Pitman Publishing, 1984.

[2] Based on: K. Pajunen: A Stakeholder Framework for Analysis of Inter-Organizational Relationships in a Crisis Situation: A Historical Case Study Illustration, EBHA Annual Congress, Helsinki 2002.

Figure 1. Relations between stakeholders and a company



Source: K. Pajunen: A Stakeholder Framework for Analysis of Inter-Organizational Relationships in a Crisis Situation: A Historical Case Study Illustration, EBHA Annual Congress, Helsinki 2002.

Another stage of a successful restructuring should focus on improving contacts with stakeholders which are a precondition for the future development of the company. Management of stakeholders is an element of the strategic restructuring process, since it not only facilitates the identification of stakeholders and their interests, but also enables to define activities needed concerning key stakeholders. The activities should lead to improving the involvement of those stakeholders which are potential beneficiaries of the restructuring process and reducing negative reaction of those who are against the process. While restructuring a company, the management of stakeholders involves looking for a consensus between interests of many stakeholders, a consensus which determines a successful restructuring program, maximizing benefits and minimizing loss for particular group of stakeholders.

In general the methodology of the stakeholders management in the process of restructuring can be divided into the following stages:

1. Identifying stakeholders, in particular those playing a key role in restructuring,
2. Analyzing and diagnosing the stakeholders,
3. Formulating relevant strategies of dealing with the stakeholders, and
4. Implementing the strategies.

After identifying the main problems and defining relations between causes and effects, further attention should focus on **who** remains under the influence of the problems, as well as roles and interests of various parties involved. When identifying stakeholders the following questions need to be answered: Whose problem is it? Who benefits from the situation?[3]. Usually the problem concerns external stakeholders (e.g. creditors, suppliers) and internal

[3] AusGuidelines: the logical framework approach, AusAid – the Australian Government's overseas aid program, 2000. www. ausaid.gov.au/ausguide/ausguidelines.html

ones (e.g. Board, employees).

Identifying the impact of stakeholders

In a stakeholder analysis, impact or power of a stakeholder is defined as the extent to which they are able to persuade, induce, or coerce others into following certain courses of action. There are several ways to exert such power, for instance by direct authority, lobbying or exerting a dominant market position. The power of stakeholders can base on various **sources**[4]:

Figure 2. Identifying the impact of stakeholders

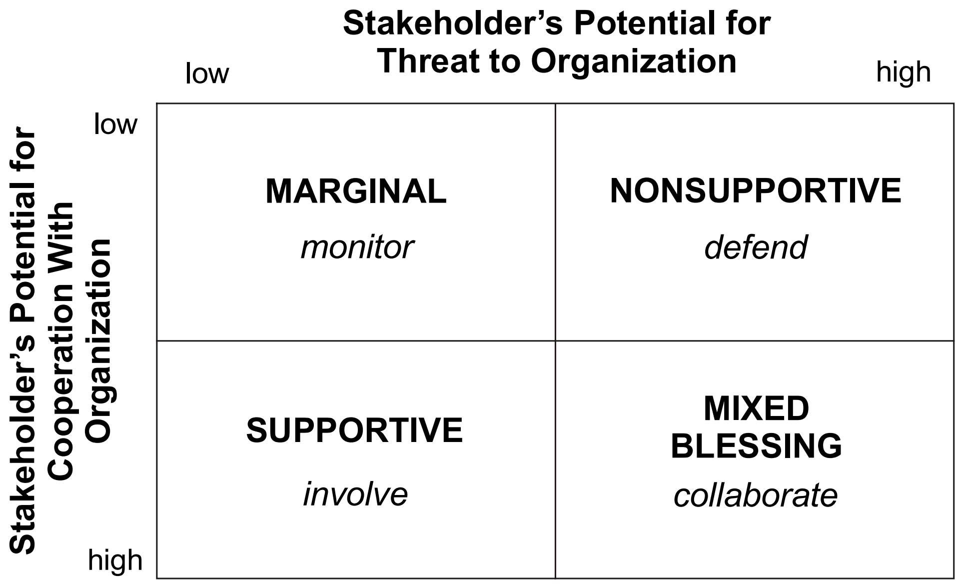
Internal Stakeholders	External Stakeholders
- Hierarchy (formal power) e.g. authority, senior position	- Control of strategic resources e.g. monopolistic supplier
- Influence (informal power) e.g. leadership style	- Involvement in strategy implementation e.g. strategic partners in distribution channels
- Control of strategic resources e.g. responsibility for strategic products	- Possession of knowledge and skills e.g. cooperation partners, subcontractors
- Possession of knowledge and skills e.g. expert knowledge that forms the organizations core competence	- Through internal links e.g. networking
- Control of the environment e.g. network of relationships to external stakeholders	
- Involvement in strategy implementation e.g. as a change agent or responsibility for strategic projects	

The power of stakeholders can grow from different sources. Therefore, it might be helpful to look out for visible signs of power. In process of restructuring it is obliged to apprehend enterprise source of authority, in order to be able affect him. In case of definitive stakeholders of restructuring process (i.e. creditors - banks and suppliers), sources of their authorities are all mentioned in principle highly.

While analyzing and diagnosing, the party managing the process of restructuring look for answers to the following questions: In what way may a given stakeholder benefit (or lose)? And What can be a possible reaction to the restructuring program? The notion of stakeholders encompasses both organizations benefiting from restructuring (beneficiaries) which react in a positive manner, and organizations which lose due to restructuring, and their reaction will always be negative. A useful tool for diagnosing can be the qualification of stakeholders according to two parameters: namely the potential for threat and the potential for cooperation. Depending on the two parameters we define stakeholders as marginal, supportive, non-supportive and showing a moderate support (or dissatisfaction). This stage of the process results in defining the hierarchy of stakeholders and their individual impact on the restructuring of the company. These groups of stakeholders and possible strategies are presented in Figure 3.

[4] D. Recklies, Recklies Management Project GmbH, www.themanager.org, April 2001.

Figure 3. Groups of stakeholders and possible strategies



Source: Savage, Grant T. et al. (1991): Strategies for Assessing and Managing Organizational Stakeholders, in: Academy of Management Executive, 5. Jg., H. 2, 1991, S. 61-75

Other useful instrument in stakeholders analysis is classic classification of stakeholders R.Mitchella.

From the point of view of a possibility to influence the environment one can classify stakeholders according to the following criteria:

a) possibility to positively (supportive) or negatively (negating or anticipating) influence processes carried into effect by an enterprise, (so called social legitimacy) that is bound to the system of collectively acceptable rules, values and beliefs;
b) power understood as possibility to influence attitudes and behaviour of single persons or groups of persons (power);
c) responsiveness of an organisation to stakeholders' demands and speed of reaction of an enterprise (urgency).

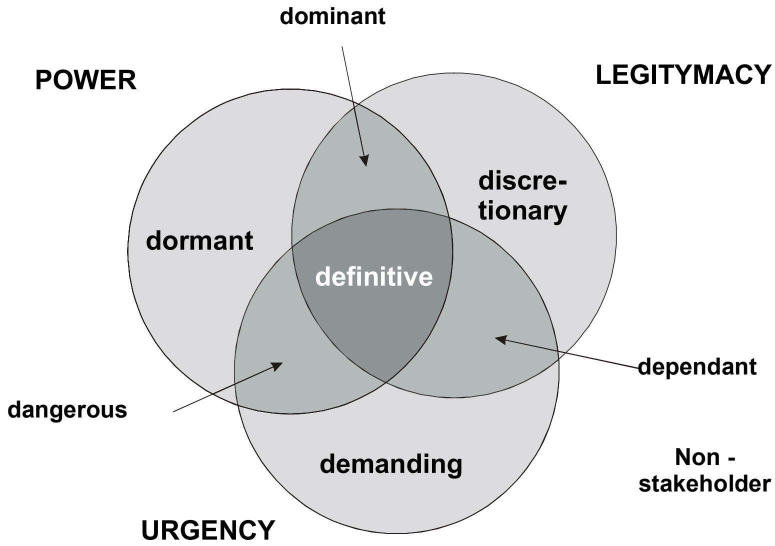
On the basis of these criteria one can distinguish seven types of stakeholders in an enterprise[5]. Graphically they are depicted in the Figure 4.

1. Dormant Stakeholder - has just the power and a possibility to influence a pressure on realisation of processes in an enterprise. An enterprise doesn't have to take any actions towards such a stakeholder. Moreover, a dormant stakeholder doesn't take any positive (supporting) actions nor any negative (destructive from the point of view of achieving of goals) ones.
2. Dominant stakeholder - has both power, i.e. possibility to influence achieving of the goals of an enterprise, as well as legitimacy, so he may influence activities of an enterprise in a negative or a positive manner. An enterprise however doesn't need to, or doesn't have possibility to influence such a stakeholder.
3. Discretionary stakeholder - is legitimate, i.e. has possibility to influence an enterprise both in a positive and in a negative way. He doesn't have any power, so an enterprise

[5] Based on: R. Mitchell, B. Agle, D. Wood: Towards a Theory of Stakeholder Identification and Salience: Defining the Principle of Who and What Really Counts. „Academy of Management Review" 1997, nr 22, s. 874.

doesn't need to take any actions towards such a stakeholder.
4. Definitive stakeholder - is legitimate, so influences an enterprise in a negative or a positive way. An enterprise needs to take intensified actions towards such a stakeholder.
5. Dependant stakeholder - has legitimacy, i.e. influences (in a positive or a negative way) an enterprise. He requires actions of an enterprise.
6. Dangerous stakeholder - has power, i.e. supports or torpedoes innovative policy of an enterprise and the enterprise is obliged to take actions toward such a stakeholder.
7. Demanding stakeholder - has no power and no legitimacy in a capacity of an enterprise but an enterprise must take actions towards such a stakeholder.

Figure 4. Stakeholders typology



Source: R. Mitchell, B. Agle, D. Wood: Towards a Theory of Stakeholder Identification and Salience: Defining the Principle of Who and What Really Counts. „Academy of Management Review” 1997, nr 22, s. 874.

For determination of potential strategy in accordance with given stakeholders in process of restructuring for one of highly mentioned category. In case of bank and suppliers process of restructuring they present kind of stakeholders granting at least two criteria, I.e. they have authorities (according to sources placed in table) and they are legalized regulations right which defines them participation and right as law in process of restructuring of enterprise. These subjects can become also “definitive stakeholder” if can execute immediately right (e.g. demand for expression of (return of) debt). Manner of behavior accordance with stakeholders has been defined in it over.

For example, banks can employ in accordance with debtor in process of financial restructuring following strategy:

- strategy of engagement - aided process of sanction of enterprise
- strategy of confrontation - relying on exemption of (credit center (means) in such range, there is possible in that
- strategy of expecting - relying on monitoring debtor and better insurance of credit without active participation in processes of sanction

The diagnosing of groups of stakeholders leads to formulating a relevant strategy toward each group. Depending on the specific character of stakeholders from the point of view of potential for cooperation and threat to the organization, we may distinguish the following strategies:

- In the case of marginal stakeholders: monitoring the activity of a stakeholder, following continuously the evolution of interests,
- In the case of non-supportive stakeholders: a defense strategy,
- In the case of supportive stakeholders: strategy of involving in particular kind of activity of the organization,
- In the case of stakeholders showing limited support (mixed blessing): collaboration.

The final stage is implementing the strategy toward stakeholders. The implementation should be based on the following principles, which at the same time constitute a set of guidelines for managers on how to deal with stakeholders during the process of restructuring:

- managers should acknowledge and actively monitor the concerns of all legitimate stakeholders, and should take their interests appropriately into account in decision-making and operations,
- managers should listen to and openly communicate with stakeholders about their respective concerns and contributions, and about the risks that they assume because of their involvement with the corporation.
- managers should recognize the interdependence of efforts and rewards among stakeholders, and should attempt to achieve a fair distribution of the benefits and burdens of corporate activity among them, taking into account their respective risks and vulnerabilities.
- managers should adopt processes and modes of behavior that are sensitive to the concerns and capabilities of each stakeholder constituency.
- managers should work cooperatively with other entities, both public and private, to insure that risks and harms arising from corporate activities are minimized and, where they cannot be avoided, appropriately compensated.
- managers should avoid altogether activities that might jeopardize inalienable human rights (e.g., the right to life) or give rise to risks which, if clearly understood, would be patently unacceptable to relevant stakeholders.
- managers should acknowledge the potential conflicts between (a) their own role as corporate stakeholders, and (b) their legal and moral responsibilities for the interests of stakeholders, and should address such conflicts through open communication, appropriate reporting and incentive systems and, where necessary, third party review[6].

Undoubtedly, stakeholders play an important role in the process of restructuring. Rehabilitation of a company and its further development depend on the cooperation between managers responsible for restructuring and stakeholders, and working out common solutions. The development of a corporation translates into the growth of its value for shareholders and tax revenue for the state and new sales markets for suppliers.

REFERENCES:

1. AusGuidelines: the logical framework approach, AusAid – the Australian Government’s overseas aid program, 2000. www. ausaid.gov.au/ausguide/ausguidelines.html.
2. Freeman R.E., (1984), Strategic management: A stakeholder approach, Pitman Publishing, Boston.
3. Mitchell R., Agle B., Wood D., (1997), Towards a Theory of Stakeholder Identification

[6] Full description of all principles of managing stakeholders: materials by Clarkson Centre for Ethics & Board Effectiveness, http://www.rotman.utoronto.ca/CCBE/.

and Salience: Defining the Principle of Who and What Really Counts, Academy of Management Review nr 22.

4. Pajunen K., (2002), A Stakeholder Framework for Analysis of Inter-Organizational Relationships in a Crisis Situation: A Historical Case Study Illustration, EBHA Annual Congress, Helsinki.
5. Recklies D., Recklies, (2001), Management Project GmbH, www.themanager.org, April.
6. Savage, Grant T. et al., (1991), Strategies for Assessing and Managing Organizational Stakeholders, in: Academy of Management Executive, 5. Jg., H. 2.