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Innovative ways of raising funds and adding value: A stakeholder approach to whole business securitization

Tuulikki Haaranen [a], Tahir M. Nisar [b,*]

[a] *Arcada University of Applied Sciences, Jan-Magnus Janssonin aukio 1, 00550 Helsinki, Finland*
[b] *School of Management, University of Southampton, Southampton SO17 1BJ, UK*

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Abstract Whole business (WB) securitization is a corporate fundraising strategy that allows companies to realize the full value of their operating assets in cooperation with their stakeholders. In a WB securitization, the company raises funds by issuing securitization bonds backed by its operating assets. A characteristic feature of this funding strategy is that it allows investors to impose operating conditions which obligate the company to develop its business strategy and operations. Hence, investors can influence the branding and customer service practices, as well as the stakeholder relationships of the company. Herein, we outline how managers of the securitized assets and investors can add value by adopting a stakeholder approach to whole business securitization.

1. Going beyond the traditional funding route

Whole business (WB) *securitization*, also known as intellectual property securitization, is the process of raising debt secured by all or substantial parts of a company's operating assets. The trend was originally set when, realizing that intellectual property rights to music are an important source of receivables, rock musician David Bowie and soul musician James Brown sold bonds backed by expected royalties.

WB securitization in its present form requires that the company, or *originator*, issue securitization bonds supported by its operating assets (Hill, 2002). The assumption is that if securitized assets are trademarks, copyrights, patents, or other intangibles, the full securitization value of these assets is dependent upon the company's ongoing operations. When WB is securitized, the originator will have an obligation to exploit underlying operating assets and, as part of the contract, take specific steps to develop its operations. This is underscored by the fact that "corporate securitizations can

* Corresponding author.
E-mail addresses: tuulikki.haaranen@arcada.fi (T. Haaranen), t.m.nisar@soton.ac.uk (T.M. Nisar).

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include many operating components, such as supply chain management, manufacturing, marketing, and distribution, which are necessary to the ongoing successful operation of a business'' (S&P, 2003).

Consider, for example, an airport; claims on the basis of earnings from landing and takeoff fees could be securitized. In such a case, it would be incumbent upon airport management to not only maintain facilities to the requisite standards, but also make investments toward fulfilling its innate potential of customer service. Now consider a franchise asset securitization; here, the 'servicing' function may include product development and marketing, negotiating contracts with suppliers or key customers, brand management and quality control, training, and monitoring/maintaining equipment.

WB securitization thus differs from traditional asset-backed securitization (ABS) in that the latter does not require the originator to develop its underlying assets (Schwarcz & Ford, 2003). Rather, the asset originator servicing the securitized receivables and loans is merely required to maintain the quality of the assets. In a mortgage securitization, for example, the contract stipulates all future payments to be made by the mortgage holder, and the sponsor does not have any further requirements toward the mortgage holder.

The dependence of WB securitization on a company's operating assets means that the originator can raise funds in more innovative ways, and thus obtain benefits for its stakeholders. For instance, a business may find that it could reduce its cost of funding by pricing its intangible assets more efficiently. Hertz's securitization transaction was completed as part of a buyout in 2005, and the cost of corporate debt used in the Hertz acquisition was much greater than its cost of financing via WB securitization. Hertz paid much higher interest on its corporate debt than what it paid on its securitization bonds. Capital raised via WB securitization can be used for different purposes such as expanding a company's core business by acquisitions, reinvesting in business, reducing leverage, or providing shareholder benefit. Such benefits generally accrue because securitization reduces transaction and information costs between borrowers and lenders. The creation of a more cost-effective capital structure is a goal that all companies strive to achieve through various innovative means. As such, it is no surprise that companies now routinely consider WB securitization along with other traditional approaches when raising new funding.

Herein, we aim to provide a discussion of the role of WB securitization in the process of creating value for companies of securitized assets and their various sets of stakeholders. Extant research on securitization has mostly been undertaken from a financial perspective and focuses on how ABS can be explained by factors such as regulatory changes or involuntary creditors, or factors external to the firm (Jones, Tett, & Davies, 2008). However, as indicated, WB securitization involves changes in the organizational structure and value creation logic of the firm and therefore may have implications to the management practice. In particular, company management will need to ensure an alignment of various stakeholders' interests so as to achieve business development goals. This article examines these questions by deploying stakeholder and value cocreation views. Using existing information about the securitizations of Hertz, Dunkin' Brands, and Domino's Pizza, as well as securitization policies used in the film industry, we explain how investors and companies can add value through securitization.

2. Effects of WB securitization on the organization of the firm

The securitization transaction involves financial risks linked to the intrinsic business features of an enterprise. Since securitized assets need to be continuously exploited to generate revenues with which to repay the debt, there is an additional business risk of management's inability to perform. This performance risk is different from a traditional securitization whereby the servicer is mainly tasked with collecting on existing receivables. Hence, the methods to reduce risk and incentivize managers will be under greater scrutiny in a WB securitization. A WB securitization materializes its operations through two key mechanisms: setting up a special purpose vehicle (SPV) and designing business-specific operating conditions (i.e., covenants). Both these mechanisms ensure not only that securitized assets are fully optimized, but also that the interests of investors and originators are aligned with each other. Under a securitization structure, a parent company sells its operating assets (e.g., inventories: property, plant, equipment) or rights linked to them (e.g., intellectual property rights (IPRs)) to a new legal entity—a *special purpose vehicle* (SPV), set up as a trust or limited liability company that usually operates as a subsidiary to the parent company. The basic task involves taking the company apart and reassembling the revenue-producing assets inside the SPV. Because of the isolation of the assets in a 'bankruptcy-remote' entity (i.e., the bankruptcy of the borrower does not affect the securitized assets), investors are better able to evaluate their inherent resilience.