



GIBSON DUNN

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The Art of the Spin-Off

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MCLE Certificate Information

- Most participants should anticipate receiving their certificate of attendance via email approximately four weeks following the webcast.
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Today's Panelists



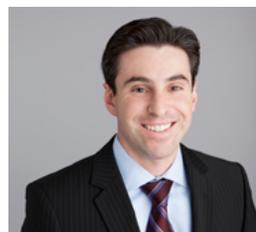
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Agenda for Today's Webinar

I. Overview of Spin-off Transactions

II. Key Separation Issues

III. Tax Planning

IV. Employment and Benefits Plans

V. Capital Markets and Corporate Governance Considerations

VI. Intellectual Property Issues

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Overview of Spin-Off Transactions

Why a Spin-Off?

Spin-Offs as Value-Enhancing Divestiture Alternative

- Companies considering divestiture of a business increasingly have looked to spin-offs
 - Attractive alternative to a traditional business unit or divisional sale
- Spin-off transactions are viewed as a means to unlock value for shareholders on a tax-free basis
 - Result in separation of divergent businesses, providing each separated business with the ability to focus solely on its own growth prospects and strategies
 - Tailor incentive compensation arrangements to the applicable business
 - Design capital structure suitable for each business
 - Shed businesses that do not fit Parent's business model and/or that may be undervalued in the market
- Spin-offs may position the separated businesses as more attractive acquisition candidates
 - Create additional potential benefits for shareholders
 - But could also make the separated businesses targets for an unsolicited takeover
- Subject to applicable tax limitations, it is possible to realize cash proceeds in connection with a spin-off
 - Conduct an initial public offering of a portion of SpinCo prior to its full separation
 - Add debt to SpinCo's capital structure, and have SpinCo pay a dividend to Parent before its separation
 - Engage in spin-off backed by financial sponsor (sponsored spin)
 - Utilize other monetization and recapitalization strategies

Separation Alternatives

Spin-Off

Steps:

- Parent transfers target business into stand-alone subsidiary (“SpinCo”)
- Parent distributes SpinCo stock to stockholders of Parent as of the record date for the spin-off
 - Note: in split-off alternative, Parent stockholders may exchange, on a *pro rata* or non-*pro rata* basis, Parent shares for SpinCo shares (typically at a discount to market to incentivize holders to tender into exchange)
- SpinCo is operated as a separate, publicly traded company

Tax:

- Tax-free to both Parent and stockholder of Parent if requirements of IRC Section 355 are met

Approvals:

- Parent stockholder approval is not typically required

Timing:

- Generally 6-12 months following initial filing

Subsidiary IPO / Spin

Steps:

- Parent transfers target business into stand-alone subsidiary (“NewCo”)
- NewCo completes initial public offering, which may include secondary sale of a portion of Parent’s interest and/or primary offering
 - Provides cash to Parent in connection with separation
- Parent’s remaining interest in NewCo is subsequently spun-off or split-off to complete separation

Tax:

- Parent must retain 80% voting control in IPO in order to ensure subsequent spin/split will be tax free

Timing:

- 12 months+ following initial filing

Sponsored Spin

Steps:

- Similar to Spin-Off, but financial sponsor invests in SpinCo contemporaneously with the Spin
 - Introduces a third party into the negotiation
 - Provides cash to Parent in connection with separation

Tax:

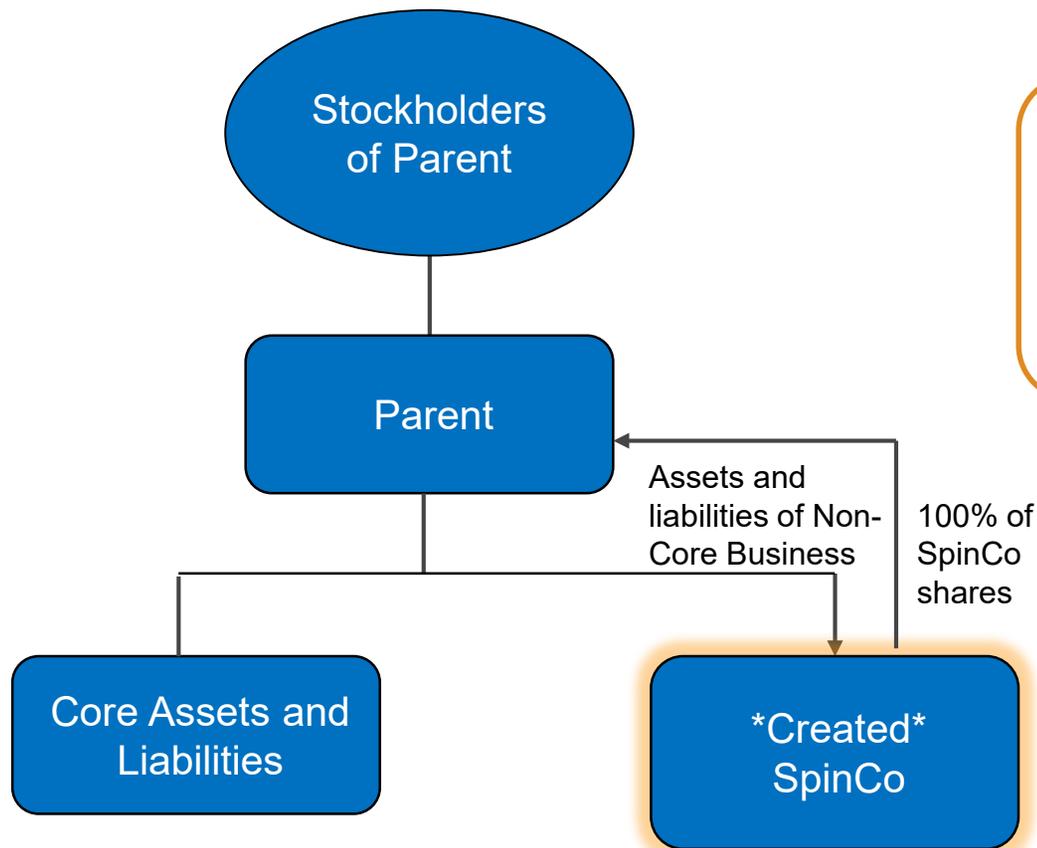
- Generally tax-free to both Parent and stockholder of Parent if requirements of IRC Section 355 are met
- Proceeds from sponsor investment Parent generally tax free

Timing:

- Similar to Spin-Off

Spin-Off: Transaction Steps

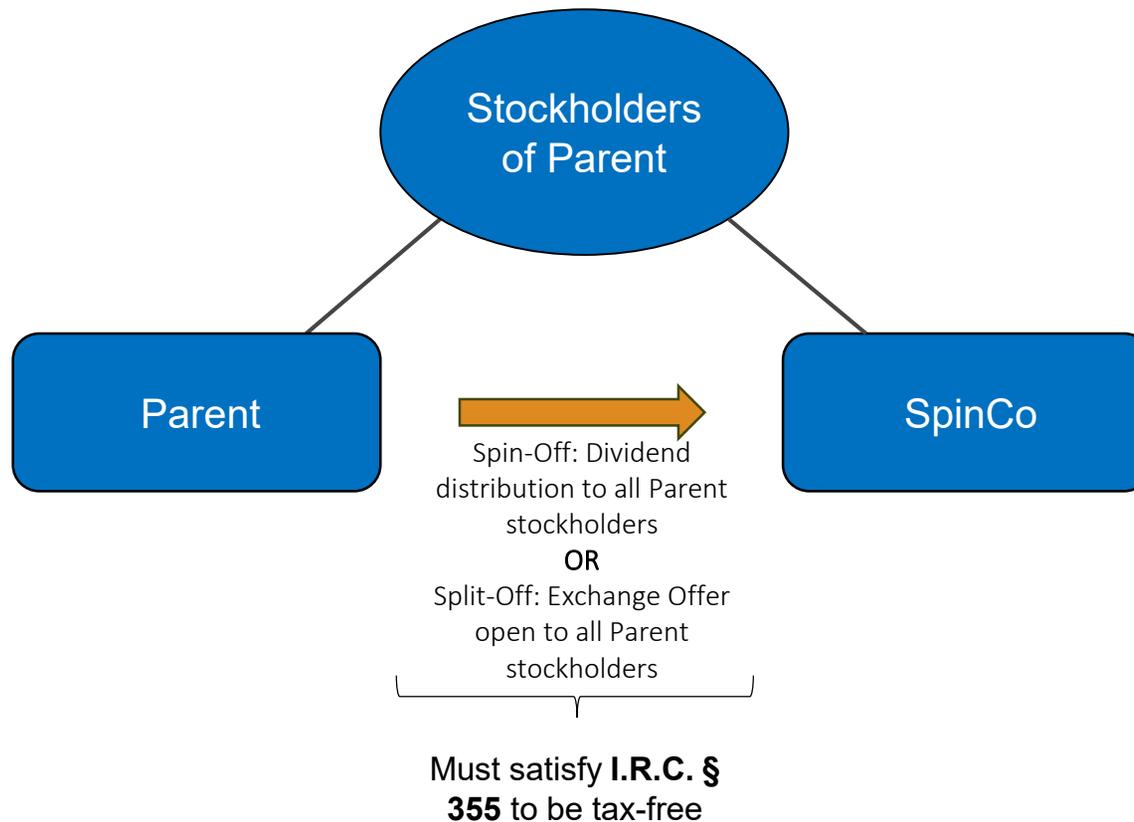
Step 1: Creation of SpinCo Subsidiary



* Step 1 assumes that the assets and liabilities of the business to be spun off are not held in a subsidiary of Parent. This step is not necessary if the business to be spun off is already held in a subsidiary of Parent.

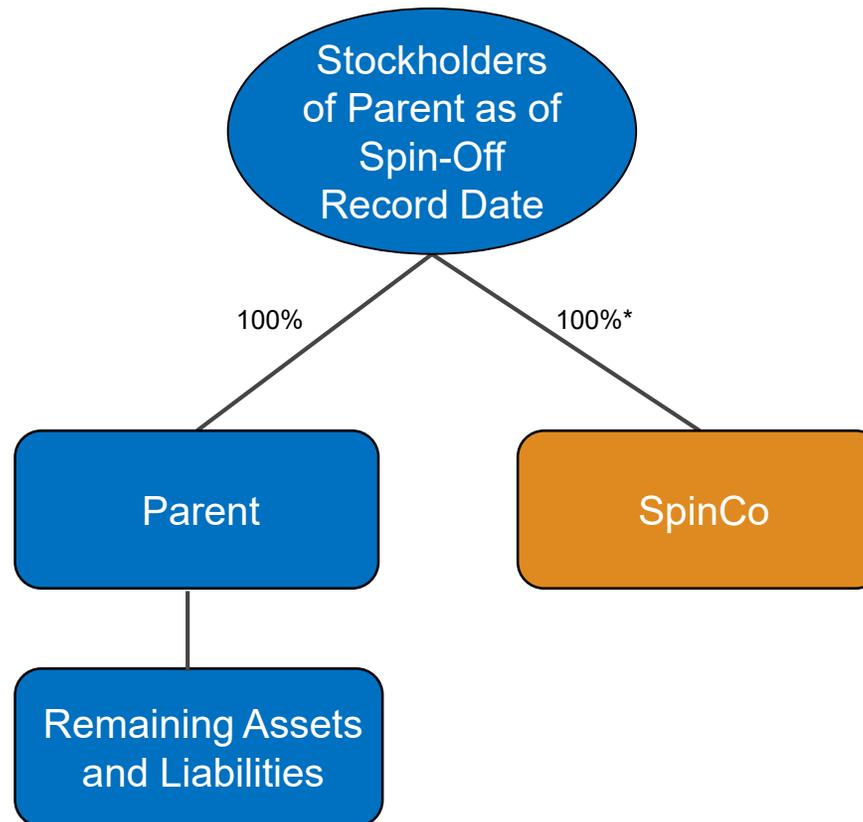
Spin-Off: Transaction Steps (cont'd)

Step 2: Distribute SpinCo to Existing Stockholders



Spin-Off: Transaction Steps (cont'd)

Step 3: End Result of Spin-Off



* Final ownership may depend on transaction structure utilized for the spin-off and whether Parent retains any equity in SpinCo. Parent must relinquish control (as defined in the Internal Revenue Code) as a result of the spin-off (stock representing 80% of voting power and at least 80% of total number of shares of all other classes of stock of SpinCo) for tax-free treatment.

Illustrative Timeline of Spin-Off Transaction

~1-6 months (depending on timing of audited financial statements and tax rulings)

~4-6 months



Initial Preparations

- Perform comprehensive internal corporate and tax analysis
- Determine transaction structure
- Audit and assessment of assets and liabilities to be transferred to SpinCo
- Establish need for solvency opinions, IRS private letter ruling and other third-party deliverables

Negotiations and Drafting

- Due diligence on Parent's and subsidiaries' documents to identify legal issues
- Negotiate and draft primary transaction agreements and ancillary agreements
- Draft Form 10
- Develop and audit SpinCo financial statements
- Coordinate SpinCo financing

Announcement

- Investor relations plan established
- Parent board (and SpinCo board, as necessary) approves transactions
- Announce transaction
- Parent files Form 8-K

Approvals and Consents

- File Form 10 with SEC, followed by SEC comment and review process
- File SpinCo listing application
- File IRS ruling request
- Obtain third-party consents or other regulatory approvals, as applicable
- Marketing of SpinCo debt, if applicable

Closing

- Form 10 declared effective by SEC
- Receive favorable IRS ruling and tax opinion
- Declare spin-off dividend
- Sign separation / distribution agreement and ancillary agreements
- Transfer assets and liabilities to SpinCo
- SpinCo shares distributed to Parent stockholders

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Key Separation Issues

Key Separation Considerations

Companies contemplating a spin-off should be aware that the documentation and implementation process can be complex, requiring significant advance preparation.

▪ Business considerations

- Establish business purpose of spin-off
- Define the scope of the businesses, assets and liabilities (including any “shared” assets and liabilities) to be separated
- Identify any commercial, indemnification and other arrangements expected to continue between the separated businesses post-spin, including ongoing shared services (legal, financial, HR, etc.)

▪ Transaction structure

- Spin-off can be coupled with a variety of monetization and recapitalization techniques
- Assess transaction alternatives and attendant costs/risks
- Indebtedness covenant analysis
 - Does the spin-off amount to a transfer of “all or substantially all” assets for purposes of Parent debt obligations
- Impact on existing material contracts
 - Assignment/change of control analysis
 - Parent guarantees, including government guarantees
- Consider need for regulatory approvals, especially in foreign jurisdictions

▪ Viability of each entity

- Fraudulent conveyance
 - Transfer of assets and liabilities to SpinCo is generally not for reasonably equivalent value
 - Transfers may be voidable if Parent and SpinCo do not meet solvency/capital requirements following the transfer
- Consider obtaining solvency opinion with respect to Parent and SpinCo post-spin
- SpinCo needs adequate resources and infrastructure to bridge transition to independence

Separation of Assets and Liabilities

Host of complex and interrelated issues to be considered, including:

- Determination of assets and liabilities to be allocated to SpinCo
- Effecting the separation of SpinCo in a cost- and tax-efficient manner
- How to separate integrated SpinCo assets/businesses from Parent's retained businesses
 - e.g., IT assets can be shared by affiliates in ways that are not immediately obvious
- Responsibility for historical SpinCo liabilities
- Arrangements regarding any shared assets and liabilities
 - Are shared asset and liability arrangements short-term or long-term?
 - On what basis will use of shared assets and responsibility for related costs be determined?
 - Who will be responsible for maintenance of shared assets and employee training?
 - How will decisions be made regarding settlement of shared liabilities?
- Allocation of benefits and burdens of contracts involving both SpinCo's assets and Parent's retained assets
- Replacement of Parent guarantees of SpinCo obligations and vice versa
- Sufficiency of SpinCo assets
 - Refers to SpinCo's capability of operating on a stand-alone basis
 - Transaction agreement may contain a representation on this point
 - Regardless of representation, parties need thorough due diligence to ensure SpinCo has necessary infrastructure and systems to operate as an independent company on "day one"
 - Transition services arrangement may be necessary

Key Separation Considerations (cont'd)

- **Tax Consequences of Spin-Off**
- **Liquidity and Capital Resources**
 - Consider capital allocation of indebtedness
 - Common for SpinCo to pay dividend to Parent in connection with a spin-off
 - Impact of any distribution or other monetization on respective capital structures of Parent and SpinCo must be assessed
- **Required Approvals**
 - No stockholder approval required under Delaware law
 - SEC registration and review of Form 10
 - Need to determine whether the spin-off would breach or require consents under material agreements
 - Need to determine whether the spin-off would impair Parent's ability to comply with its retained contracts
- **SpinCo Financial Statements**
 - Preparing GAAP financial statements may be difficult if, historically, SpinCo's business has not been separately reported
 - Availability of financial statements impacts ability to effect a transaction and transaction timing
 - Audited financial statements required for Form 10 Information Statement
 - Audited financial statements likely required for related financing transactions
- **Parent Financial Statements**
 - Parent may need to file pro forma financial statements showing the disposition of SpinCo

Key Separation Considerations (cont'd)

▪ SpinCo Controls

- Need to determine if SpinCo has necessary internal controls over financial reporting, as well as disclosure controls and procedures, to produce financial statements and reports required of reporting companies
- SpinCo may need to upgrade its systems, including purchasing computer hardware and software and hiring additional personnel for finance, accounting, information technology and legal staff

▪ Listing on an Exchange

- Need to determine if SpinCo will meet initial listing requirements
- Need to determine if Parent will meet continued listing requirements following the spin-off
 - Requirements include total shareholders, per share price, number of market makers and market value of public float

▪ Employee Matters

- Allocate management and human resources between Parent and SpinCo
- Benefits and compensation issues
- Determine treatment of equity awards in the spin-off

Role of the Board

Board Action Required

The role of the Parent board of directors in connection with a spin-off includes:

- Approve material agreements and other legal documentation
- Approve any pre-spin internal reorganization transactions
- Appoint initial public SpinCo board and senior management
 - Appointment of independent directors is typically not effective until the spin-off is completed
- Declare dividend of SpinCo stock to Parent stockholders

Director Fiduciary Duties

Directors need to be mindful of their fiduciary duties in approving the spin-off transactions, as follows:

- **Duty of Care:** directors should fully inform themselves of all material information that is reasonably available and act as reasonably prudent persons in similar situations would act
- **Duty of Loyalty:** directors must act in good faith in the honest belief that their decision is in the best interests of Parent stockholders, and their decision must not be motivated by self-interest
- Parent board's fiduciary duties are owed to *Parent* stockholders (*not* to the future stockholders of SpinCo)
- Directors' actions in approving a spin-off will generally be entitled to the benefit of the business judgment rule presumption if they have fulfilled their duties of care and loyalty

Role of the Board

Liability for Unlawful Dividends

- Under Delaware law, a corporation may pay dividends out of its “surplus” or net profits for the current or prior year
 - Parent board must conclude that the value of SpinCo stock to be dividended out does not exceed Parent’s surplus or net profits for the current or prior year
- Directors may be held personally liable under Delaware law for negligence in connection with a dividend not lawfully paid from available funds
- Directors are protected from liability for unlawful dividends made in reliance on reports of officers, employees, board committees or experts
 - Parent board should review evidence provided by Parent management with respect to surplus, and may obtain analyses/appraisals from experts to determine adequacy of surplus
 - Board should also receive viability analysis from chief financial officer of Parent with respect to each of Parent’s and SpinCo’s ability to finance its anticipated operations and capital requirements following the spin-off
 - Board should also obtain a solvency opinion from a valuation firm

In evaluating a spin-off, the Board must obtain a full picture of the value-increasing potential of the transaction as well as the attendant costs and risks, in each case weighed against transaction alternatives, including the alternative of maintaining the status quo.

Major Documents - Contracts

▪ Separation and Distribution Agreement

- Key operative document; provides for internal reorganization
- Transfer of assets and liabilities
- Distribution of SpinCo shares
- SpinCo financing arrangements
- Mutual release of historical liabilities
- Indemnification for transferred/retained liabilities
- May contain post-closing working capital adjustment mechanism

▪ Other Separation Agreements

- Tax Matters Agreement
 - Governs rights, responsibilities and obligations with respect to tax matters
- Employee Matters Agreement
 - Sets forth agreements regarding employment, compensation and benefits
- Transition Services Agreement
 - Governs services provided by Parent for limited time following spin-off

▪ Other Separation Agreements (cont'd)

- Litigation Management Agreement
 - Details transfer of litigation/investigation matters from Parent to SpinCo
- Insurance Matters Agreement
 - Allocates rights regarding insurance policies

▪ Contractual Assignments/Consents

▪ Other Ancillary Agreements (as needed)

- Manufacturing and Supply Agreement
- Real Estate Agreements
- Research and Development Agreement
- Licenses
- Other Intercompany Agreements

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Tax Planning

Tax Planning

▪ General Background

- ***Must comply with various technical requirements in Internal Revenue Code and Treasury Regulations to be tax-free.***
- ***Taxpayers often seek IRS private letter rulings on spin-offs.***
- ***IRS periodically issues guidance on ruling practice, including:***
 - Procedures for seeking rulings.
 - Issues on which it will rule.
 - Issues on which it will not rule.

Tax Planning

▪ Private Letter Rulings

• **Considerations**

- Full transaction ruling vs. significant issue ruling.
- Timing.
- Representations and information that must be provided to IRS.

• **IRS Pilot Program**

- From 2013 – 2017, IRS would not issue full transaction rulings.
- In Rev. Proc. 2017-52, IRS introduced 18-month pilot program for full transaction rulings.
- In March 2019, IRS extended pilot program indefinitely.
- IRS now encouraging taxpayers to come in for full transaction rulings.
- Rev. Proc. 2017-52 contains procedures for transactional rulings, including required “standard” representations.
- Still some no-rule areas.

Tax Planning

▪ IRS Announcement on Active Trade or Business Requirement

• ***Active Trade or Business Requirement***

- Both Parent and SpinCo must be engaged in active trade or business (“ATB”) immediately after spin-off.
- ATB must have been conducted for at least five years.
- Previously, Treasury Regulations and IRS practice required collection of income in order to qualify as ATB.
- Precluded tax-free spin-offs of some early stage and R&D-focused businesses.

Tax Planning

▪ **IRS Announcement on Active Trade or Business Requirement**

• ***IRS Chief Counsel Announcement – September 25, 2018***

- IRS announced it is studying ATB requirement for ventures that have not yet generated any operating income.
- Pending guidance, IRS will entertain requests for private letter rulings on whether activity that has not generated income qualifies as ATB.
- Guidance intended to identify factors other than income that suggest ATB.
- Factors could include:
 - Regular R&D by significant number of employees.
 - Regular R&D expenses.
 - Significant progress toward developing income-producing product.
 - Holding out business as available to enter into income-producing arrangement.
 - Actual offer or expression of interest to enter into income-producing arrangement.
 - Similarly situated businesses have entered into income-producing arrangements.

Tax Planning

▪ IRS Announcement on Active Trade or Business Requirement

• *Subsequent Developments*

- In March 2019, IRS suspended two 1957 Revenue Rulings that required income generation for a business to qualify as an ATB.
- In May 2019, IRS announced continuation of study and requested information to assist in identifying what types of entrepreneurial ventures should qualify as non-income generating ATBs.
- In February 2020, IRS released first private letter ruling under this guidance. Private Letter Ruling 202009002, limited to a narrow significant issue, states that the absence of income collection of the spun-off business does not prevent transaction from satisfying the ATB requirement.

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Employment and Benefits Plans

Retirement Plans

▪ **Defined Benefit Pension Plans**

- “Split” (if any) of the plan needs to be determined
 - Sometimes RemainCo keeps all of these obligations, especially in relatively small transactions
- If there is a split, how to allocate liabilities to retirees/deferred vested participants is critical
- What about “orphan” participants (business that employed them was sold but pension obligations retained)?

▪ **401(k)/Defined Contribution Plans**

- Often split into two plans
- If not, need to determine how to handle outstanding plan loans for RemainCo employees
- Company stock fund raises ERISA issues

▪ **Nonqualified Plans**

- These are “top hat” plans covering high-level employees and are unfunded
- Often follows same process as defined benefit/defined contribution plans

▪ **International Retirement Plans**

- Needs to be discussed with counsel – may be special issues
 - In some jurisdictions (e.g., Germany), pension plans typically are not funded

▪ **Retiree Medical Benefits**

- These typically are not funded, and can be very expensive
- Like with defined benefit pensions, allocation rules are critical

Equity Awards

- **Most Common Approach: Awards at Post-Spin Employer (“Employer Approach”)**
 - The most common approach is for all awards to be converted to awards of the post-spin employer
 - Thus, RemainCo employees continue to hold RemainCo awards (which are adjusted to reflect the spin) and SpinCo employees hold converted SpinCo awards
 - One decision point is how to treat former employees (for example, deferred RSUs)
 - One approach is for all to stay with RemainCo, even if active employees’ awards are allocated based on post-spin employer
 - Another is to have them assigned based on the individual’s last employer
- **Other Common Approach: Same as Shareholders (“Shareholder Approach”)**
 - In this approach, all grantees have awards in both companies, determined on the same basis as for shareholders
 - This introduces tax reporting and withholding complexities
 - Also, it is much more burdensome administratively – requires sharing of employee termination and other information to address forfeiture/expiration of awards
- **Mechanics**
 - For each type of award, the “intrinsic value” is preserved immediate pre- and post-spin-off
 - For RSUs and restricted stock, that just follows the same rules as stock
 - For options, the “spread” (difference between FMV of the underlying stock and the exercise price) is preserved

Other Key Considerations

▪ **Employment Liabilities Generally**

- Allocation rules for, e.g., lawsuits that impact current or former employees of both RemainCo and SpinCo

▪ **Medical Plans**

- If self-insured, allocation of incurred but not reported (IBNR) liability

▪ **Bonuses**

- How to determine for year of spin-off/who pays
- Adjustment of targets for both entities

▪ **Payroll**

- Will SpinCo have its own payroll system running no later than the spin date?

▪ **Benefit Plan Administration**

- Will RemainCo continue to provide benefit administration services to SpinCo?

▪ **Workers' Compensation/Disability Benefits**

- Allocation of liabilities

▪ **Employment Agreements**

- New agreements with key SpinCo executives?

▪ **Post-Closing SpinCo Compensation/Benefits Continuation**

- Will SpinCo be required to continue compensation and benefit levels for a specified period after the spin-off (e.g., 12 months)?

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Capital Markets and Corporate Governance

SEC Registration and Review Process

SEC Review

The SEC process is similar in scope and complexity to an IPO. The registration statement can be submitted confidentially to the SEC to minimize public scrutiny during the review process. SEC first-round comments are expected 30 days after filing.

1934 Act or 1933 Act Registration

Most spinoff transactions are required to be registered only under the 1934 Act, using Form 10. If the distribution is not *pro rata* or stockholders make an investment decision with respect to the distribution of SpinCo shares, then the transaction must be registered under the 1933 Act, using Form S-1 or S-4 (for split-off). The scope and content of required disclosure is virtually identical in either circumstance.

Key Differences Between 1933 and 1934 Act Registrations

In a 1933 Act registration, SpinCo, its directors and officers would be subject to strict securities law liability for material misstatements or omissions (with a diligence defense for directors and officers.) In a 1934 Act registration, SpinCo would be subject to 10b-5 liability and directors and officers would have more limited exposure (with stronger defenses.)

In addition, a 1933 Act registration would be subject to "gun jumping" and other communications restrictions that would affect the investor relations process by subjecting it to greater potential liability and SEC filing requirements.

Form 10 / Information Statement

In a 1934 Act spin registration, disclosure is contained in an "Information Statement" filed as exhibit to the Form 10. Once SEC review is complete and the record date for distribution is established, the Information Statement is distributed to SpinCo stockholders. "Notice and Access" delivery is available and can provide substantial saving on printing and mailing costs if transaction timing permits. Form 10 is not required to be signed by directors, does not require an accountant's consent and does not require SEC filing fees.

Preparing to be Public

Goal: Position business to be well received and perform positively over the long term

Product: Preparation of key registration document requires collaboration between management, many parts of the business, bankers and counsel

- Preliminary structuring matters
- Prepare audited standalone financials and pro-formas
- Debt and finance arrangements
- Board composition and corporate governance
- Develop investor relations messaging

Process: Multiple workstreams proceeding concurrently and touching all parts of the company

Notes on the Process

Significant planning and preparation:

- Extensive company effort to draft SEC disclosure document, prepare financial statements, collect due diligence
- Careful coordination among management, investment bankers, auditors, legal counsel and others is important throughout process

Anticipating and addressing issues early improves execution:

- Advance planning can help speed process, allowing access to a broader market window and minimizing distraction of management and disruption of underlying business
- Drafting and diligence prior to SEC filing can take at least one to two months; SEC review process can take three months (or, in the event of significant issues, longer)
- SEC comment process requires multiple rounds of quick turnaround on complicated issues with input from many stakeholders

Issues to consider and address in advance:

- Accounting, internal control, communications strategy, corporate housekeeping
- **Burden on accounting staff is especially intense**
- Time required to prepare financial statements can be result in delays/lengthen timeline

Separation Debt Financing – Overview

In connection with the separation, debt capital structure of SpinCo must be established; pay down or “transfer” of Parent debt rebalances debt load between Parent and SpinCo

- Debt capitalization typically completed prior to separation
- Considerations
 - Timing
 - Registered vs. unregistered offering
 - Form of the transaction(s)
 - Leveraging Form 10 process and documentation for the debt offering
 - Special terms of the debt
- Essential due diligence for any separation transaction: review of the “merger covenant” (“All or Substantially All” or “AOSA”) in Parent indenture.
 - AOSA covenant prohibits the disposal of “all or substantially all” of the assets of the obligor of the debt unless all assets conveyed to a single acquirer that assumes the debt obligation.

Separation Debt Financing – Form of the Transaction(s)

<i>New Issue + Repurchase</i>	<i>Par-for-Par Exchange Offer</i>	<i>Intermediated Exchange</i>
<ul style="list-style-type: none"> • New bonds issued by SpinCo for cash • Special dividend to Parent • Redemption and/or tender offer by Parent for existing bonds • Offering document based on Form 10 • Redemption or Offer to Purchase 	<ul style="list-style-type: none"> • SpinCo offers to exchange new bonds for existing Parent bonds • Cash premium paid to participating bondholders • No cash proceeds to SpinCo • Offering document based on Form 10 	<ul style="list-style-type: none"> • Tender offer by underwriters for existing Parent bonds • Underwriters agree to exchange tendered bonds for new SpinCo bonds • New SpinCo bonds sold by underwriters for cash • No cash proceeds to SpinCo • Offer to Purchase (used by underwriters) • Offering document based on Form 10

Separation Debt Financing – Details

Disclosure in bond offering will require:

- Business description, selected financial data, MD&A and risk factors copied from the Form 10 (either registered or unregistered offering)
- Description of the Notes typically based on Parent precedent and comparable bond offerings
- Transaction-specific disclosure (e.g. Description of the Exchange Offer and Description of the Differences between the Notes in a Par-for-Par Exchange)
- Initial purchasers and counsel due diligence

In an offering prior to completion of the separation, bond purchasers may expect certain *special provisions*, including:

- Parent guarantee of the bonds, which is automatically and unconditionally released upon completion of the Spin
- Special Mandatory Redemption in the event the Spin is not completed by specified date
 - Typically a 1% premium paid at redemption
 - Escrow of the proceeds no longer customary due to complexity and cost considerations

Corporate Governance Considerations

■ Governance Structure

- Constituent documents must be appropriate for a public company
- Rather than replicating Parent's governance structure, consider SpinCo's unique stance as a newly public company
 - SpinCo is likely to be smaller and potentially more vulnerable to activists
 - It is typical (and easier) for newly public companies to implement anti-takeover protections, such as classified board, for cause removal, supermajority provisions, no stockholder written consent or special meeting right, etc.
 - BUT consider the reaction of SpinCo's shareholder base
 - Initial vs. later impact of large institutional investors and proxy advisory firms
 - This may be less of a concern in a subsidiary IPO spin as long as SpinCo remains "controlled" post-IPO
 - Parent may also feel pressure to set up a "best-in-governance" SpinCo and/or maintain control (depending on the type of spin)

SpinCo's structure and governance must reflect, like Parent, a fully self-sufficient, operational public company; but there is also an opportunity for a "fresh start." Status as a "controlled" vs. "non-controlled" company is an important consideration.

Corporate Governance Considerations (cont.)

■ Board composition

- Generally desirable to choose individuals with knowledge of the business being spun off
- The Parent board and the management team are likely to be very interested in who will serve on SpinCo's board of directors
- Parent may continue to have nomination rights in subsidiary IPOs/spin-offs but usually does not have any nomination rights in Form 10 spin-offs (see next slide)
- To the extent SpinCo will need to have an entirely independent board and independent committees within one year post-spin, timing becomes even more important
- Diversity, qualifications and expertise (including that of an audit committee expert) as well as overboarding are important considerations
- Start considering post-spin board schedule early to maximize post-spin participation and attendance

Corporate Governance Considerations (cont.)

- Board composition (cont.)
 - Stock exchange requirements regarding independence of board and committee members
 - Form 10 Spin: Generally, SpinCo will have a one-year grace period to comply
 - Form S-1 Spin: Generally, Parent maintains control for some period of time post-IPO
 - If Parent owns more than 50% of voting power after the IPO, SpinCo will be a “controlled company”
 - As such, SpinCo will be exempt from the board and committee independence requirements (other than the audit committee independence requirements) and will then have a one-year grace period to comply after the loss of controlled company status

Corporate Governance Considerations (cont.)

■ Board composition (cont.)

- Overlapping directors (SpinCo/Parent) – more typical in a Form S-1 spin
 - Conflicts of interest—Directors who owe fiduciary duties to both Parent and SpinCo should not participate in decisions at either company about arrangements between them
 - Corporate opportunities doctrine—Issues could arise if Parent and SpinCo businesses overlap
 - Consider addressing fiduciaries' obligations to present different categories of opportunities to each company in separation agreement and governing documents
 - Where there are overlapping directors, certificates of incorporation often include a corporate opportunity waiver for such directors
 - Don't forget Section 8 of Clayton Act – Bars companies that engage in competing businesses from having overlapping directors
- Nomination rights
 - Form 10 Spin: Generally, Parent does not have any board and/or committee nomination rights
 - Form S-1 Spin: Parent may have some board and/or committee nomination rights post-IPO depending on level of control (similar to sponsor-backed IPOs) with such rights eventually going away as the level of control decreases below a certain percentage of ownership

Corporate Governance Considerations (cont.)

■ Other Considerations

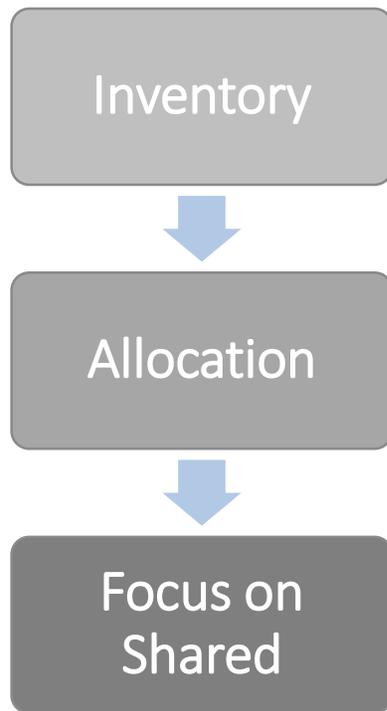
- Major transaction approval rights
 - This comes up in subsidiary IPOs/spin-offs (as compared to Form 10 spin-offs)
- Other anti-takeover protections
 - Synthetic 203 provisions, stockholder special meeting/written consent rights, etc.
- Related person/party transactions
 - Intra-company transactions may become related person/party transactions post-spin
- Consider timing of the first annual meeting of stockholders
 - There are both listing stock exchange and state law considerations
- Not immune from shareholder proposals in year 1
- Proxy advisory firms
 - Proxy advisory firms have policies that generally disfavor various anti-takeover measures
 - While their voting recommendations may be less important for a “controlled company,” they could have significant impact at non-controlled companies
 - Consider reputational impact for directors as well

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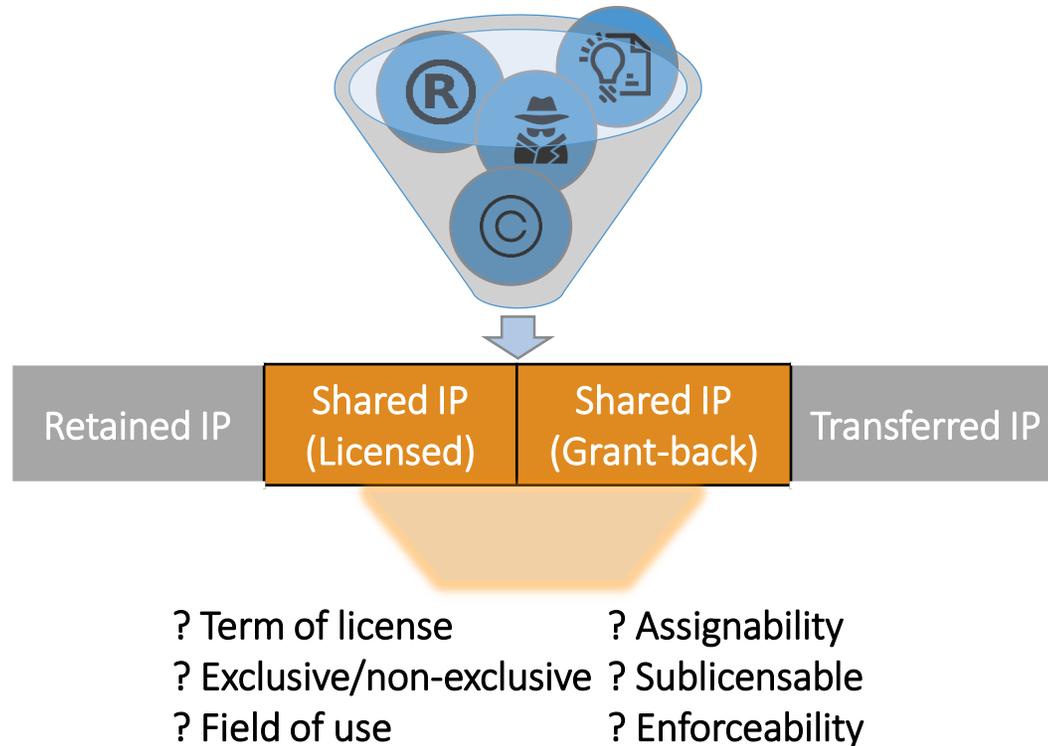
Intellectual Property Issues

Inventory and Allocation of IP in Spin-Out

High-Level Process



Intellectual Property

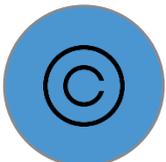


Identify early in process IP that will stay with parent, will be transferred to spin-out, and will be shared by the parties

Key Terms for Shared IP

Key Terms

Type of IP



	Term of License	Exclusive / Non-Exclusive	Field of Use	Assignability	Sublicensable	Enforceability
Registered Trademark (R)						
Patent						
Trade Secret						
Copyright (C)						

Address Key Terms for each Type of IP - balance setting up spinco for success vs. retaining value for parent

Less negotiated

Occasionally negotiated

Often negotiated

Trademarks and Trade Names

As soon as the parent makes a decision to spin out a business unit, it should consider whether the spinco will require the use of corporate names and related trademarks

- Marks may/may not represent value to Buyer/Spinco
- Potential for royalty
- If rebranding, Buyer/Spinco needs sufficient time to:
 - Conduct trademark clearances
 - Prepare/file new trademark applications
 - Secure domain name

Patents and Trade Secrets

A spin out transaction typically involves the spin out of a business that uses patents and trade secret rights that are also used by the parent and its retained businesses

- Consider whether to license or sell
- Licensed patents and trade secrets need to carefully consider appropriate field of use
- Sold patents and trade secrets need to consider standard for sale (e.g., “used by”, “primarily used by”, “exclusively used by”); potentially requires a grant back license
- Be careful of de facto non-compete with exclusive licenses

Software Licenses

Software contracts are typically held by the corporate parent so that software is available for use by all divisions

- Software licenses often prevent use by a third party (e.g., SpinCo)
- Consider “mirroring” certain critical software licenses
- Buyer/SpinCo needs to factor in re-licensing cost to purchase price
- Parent may be entitled to reduction in price if user base is reduced
- Do not dismiss shrink-wrap!

Transition Services – TSA

Spin-outs typically need certain shared services to continue to be provided for a period of time after the spin

- TSA provides mechanism to ensure continuity of service
- Provides mechanism for wind-down of services
- *A temporary* provision of services – limited in duration
- At-cost pricing / no risk premium
- No performance guarantees / limited liability to parent
- Wide variety of services potential for TSA: IT support, finance and accounting, app. development and maintenance, supply chain, treasury, facilities (beware payroll!!!)

Upcoming Programs

Upcoming Programs

- February 2 [Navigating the Minefield of Dodd-Frank's Whistleblower Provisions](#)
- February 4 [White Collar Enforcement Outlook 2021 – Sanctions/Export Controls, AML and Healthcare Fraud](#)
- February 23 [17th Annual Challenges in Compliance and Corporate Governance Webcast](#)
- February 25 [Implementing Successful Carve-Out Transactions](#)

Resources

- [Gibson Dunn Mergers & Acquisitions Practice Group](#)
- [Gibson Dunn Webcasts \(CLE Credit Available\)](#)