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Maximizing Value From Your Corporate Carveout: Lessons Learned From the Front Lines

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Preliminary Considerations in a Carveout

Putting Together the Pieces: What Are We Going to Divest?

Transaction Perimeter

- Defining scope of carved out business (the “Business”)
 - Determine assets required to conduct the Business
 - Any assets necessary to conduct both the Business and your retained businesses?
 - Restrictions on the ability to transfer assets to be divested (*i.e.*, third party consents / structural impediments)?
 - Determine whether any historical liabilities should be included in the divestiture
- Determine whether any new legal entities need to be created to effect transfer of assets and liabilities
- Management / employees to be transferred

Key Issues

- Identification of assets / liabilities and completion of any requisite internal reorganization
- Standalone financial statements
- Regulatory and third-party consents
- Intercompany arrangements
- Employment issues (particular sensitivity in carveouts in that employee support required; potential for shifting loyalties; partitioning of employee base)



Separation of Assets and Liabilities

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

- Determination of assets and liabilities to be allocated to the Business
- Effecting the separation of the Business in a cost and tax-efficient manner
- How to separate integrated Business assets/operations from retained businesses
 - e.g., IT assets can be shared by affiliates in ways that are not immediately obvious
- Responsibility for historical 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 Business assets and retained assets
- Replacement of parent guarantees of Business obligations and vice versa
- Sufficiency of assets
 - Refers to Business'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 Business has necessary infrastructure and systems to operate as an independent company on "day one"
 - Transition services arrangement may be necessary

Preliminary Considerations in a Carveout

How Do We Market What We Are Going to Divest?

Standalone Financial Statements

- Standalone historical financial statements will provide touchstone for potential buyers' evaluation of the Business
 - Financial statements adequate for this purpose are critical
 - Necessary for buyer to conduct financial due diligence
 - Likely necessary for buyer to obtain bank or public debt financing
- Consider extent to which the Business unit has been separately reported and feasibility of having existing financials audited
- Consider required adjustments / costs to be incorporated into financial statements and projections to reflect the Business as standalone
 - Challenge of allocating entity-wide assets, operational expenses and revenues to stand-alone business
 - Projections for the Business will be necessary for buyer to formulate a purchase price

Key Issues

- Required adjustments to historical financials to reflect standalone costs / dis-synergies
- Audited v. Unaudited
- Time periods to cover
- Compliance with SEC requirements



Preliminary Considerations in a Carveout

Transaction Structure

- Sale of entity (*i.e.*, stock purchase or merger agreement)*
 - Determine whether any new legal entities need to be created to effect transfer of assets and liabilities
 - Considerations include (i) timing; (ii) third party consents and approvals; (iii) whether you would want the Business segregated into separate entity in the event sale process is unsuccessful; and (iv) tax consequences
- Sale of assets
 - Asset sale may add legal complexity
 - Assignment of specific assets / contracts may trigger additional third party consents
- Spin-Off / Dividend
 - Reverse Morris Trust transaction (spin-off + merger)

Preliminary Considerations in a Carveout

Intercompany Arrangements

- Identify assets utilized in both the Business and the retained businesses
 - Enterprise-wide contracts / parent guarantees / financing arrangements
 - Intellectual property / brand names
 - Shared real property / insurance coverage
 - Management / corporate functions (i.e., HR, IT, legal, accounting, procurement, etc.)
- Identify arrangements between the Business and the retained businesses that should survive divestiture
 - Are existing arrangements documented and on arm's-length terms?
- Short or long-term agreements (i.e., TSA, Reverse TSA, Shared Services Agreement, IP Licenses, other commercial arrangements, etc.) may increase marketability of the Business and may need to be negotiated in connection with transaction

Key Documents / Workstreams

Transaction Documents

- Acquisition Agreement / SDA
- Disclosure Schedules
- Transition Services Agreement
- Reverse Transition Services Agreement
- Sublease
- Intellectual Property Licenses
- Other Commercial Agreements
- Contract Notices / Consents

Board Materials

- Board updates regarding transaction
- Fairness opinion
- Board summary / approval documents, including resolutions

Communication Materials

- Press Release
- Investor deck / script / Q&A
- Communications to customers / vendors / partners
- Internal communications, including employee communications

Regulatory Filings

- SEC filings
- Antitrust filings
- Other governmental and third party consents / notices

Operational Separation in Carveouts

Topics for Discussion



Defining the strategic objectives for the transaction



Reviewing the main drivers of separation activity

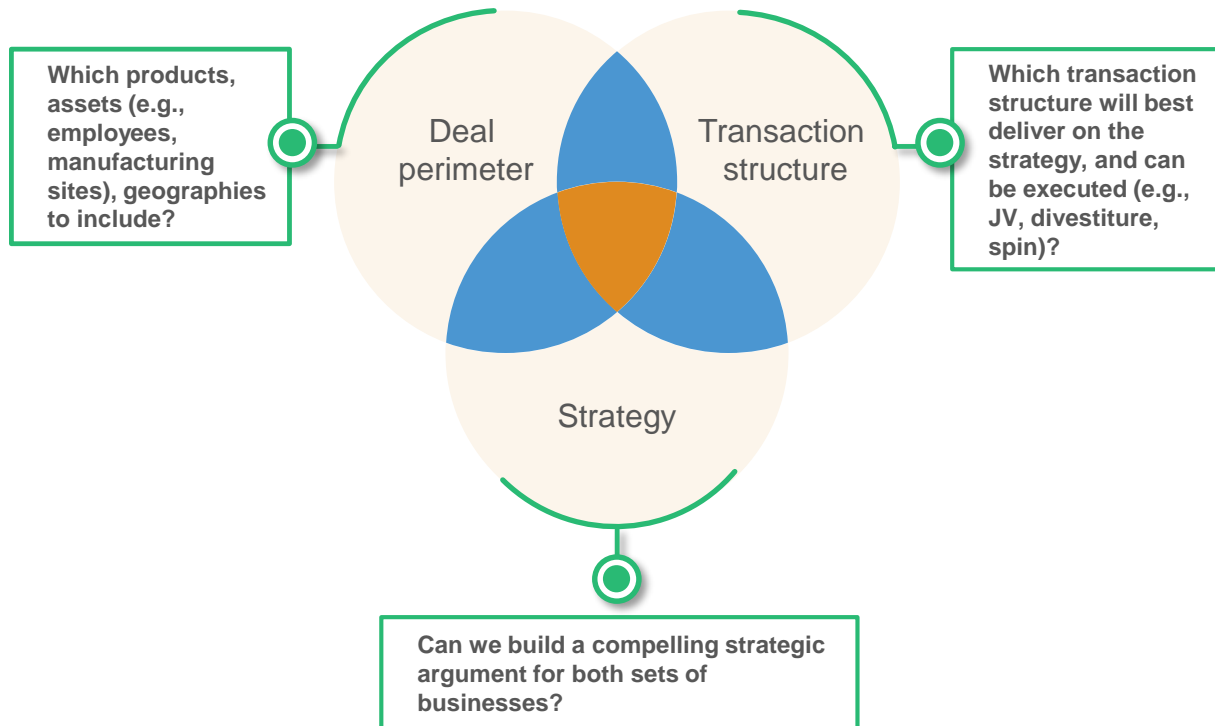


Preparing for post-carve governance & entanglement



Lessons learned and Q&A

Strategic Definition of the Transaction is Critical to Inform Operational Carveout Approach



With the aim to deliver:



Good Companies



Good Stock



Carveouts Tend to Follow Three Phases to Prepare to Close

Dedicated functional activities are not represented in this timeline

Separation Strategy & Announcement Prep

- Identify Key Risks & Assumptions
- Create process inventory to inform separation plan
- Coordinate communications to internal and external stakeholders
- Prepare A-day logistics
- Determine NewCo Org design
- Establish program governance
- Enable separation of financial reporting and related systems
- Prepare capital plans for NewCo & RemainCo

Workplanning

- Prepare global workplans & target states
- Define NewCo Purpose, Vision & Culture
- Determine NewCo growth & margin strategy
- Refine Org design as needed & engage works council
- Assign markets to Legal Entity (LE) Wave buckets
- Plan and execute the transaction (e.g. capital structure, accounting requirements, carve out analysis, & transaction-related agreements)

Implementation

- Develop & share market separation guidance
- Develop market workplan framework
- Cutover key systems & processes for major milestones
- Develop Interim Operating Models
- Monitor workplan execution
- Implement change control
- Continue Org related activities (e.g., people readiness strategy, talent selection, conveyance plan)
- Conduct roadshow
- Readiness checks & tollgates
- LE separation waves
- MA transfers
- Form 10 filing
- Registrations, licenses and permits for NewCo

Key Activities (may overlap within sub-phases)

Post-spin Planning is Critical for Both Companies to Minimize Business Disruption Post-spin



Why is Post-Spin planning important?

In a large scale spin, there will certainly be entanglement of varying degrees between companies even after spin

NewCo will be unable to set up every process at spin date due to long duration disentanglement activity and will require:

- Transition Service Agreements (TSAs), and other agreements to enable business continuity
- Additional standup and separation work (from both companies) to transition off these agreements
- Interim Operating Models (IOMs) to enable continuous supply of products for certain markets

Similarly, RemainCo will likely require NewCo support for select processes to continue being operational

Certain local markets may not be able to spin at global spin date for regulatory, legal, or other operational reasons, thus resulting in post-spin markets (PSM)



Key questions to answer

- What will be the governance / Transition Management Office structure overseeing the relationship between the two companies?
- What will be the scope of the relationship between the two companies? e.g., TSAs, MSAs, standup activities, ongoing regulatory effort, etc.
- What resourcing will be required for both companies?
- What will be the duration of the post-spin entanglement, and how does it vary by geography or process?

Lessons Learned From the “Front Lines” of a Carveout



Design your separation approach to be **consistent with RemainCo’s strategic priorities** from the transaction



Design your **global program governance** model early



Develop a plan for **post-close operating model** between the two companies



Design and execute a robust process for **regulatory strategy and supply assurance**



Develop a clear operational **strategy for deferred/entangled markets**



Build robust **people readiness** prior to close

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Daniel Angel is a partner in the New York office of Gibson, Dunn & Crutcher. Mr. Angel is Co-Chair of Gibson Dunn’s Technology Transactions Practice Group and a member of its Strategic Sourcing and Commercial Transactions Practice Group. He is a transactional attorney who has represented clients on technology-related transactions since 2003. Mr. Angel has worked with a broad variety of clients ranging from market leaders to start-ups in a wide range of industries including financial services, private equity funds, life sciences, specialty chemicals, insurance, energy and telecommunications.

Mr. Angel is ranked by Chambers and Partners for his work on corporate technology transactions. He has also been recognized by *The Best Lawyers in America*[®], *IFLR1000*, listed in *The Legal 500 U.S.* as a “Next Generation” lawyer in Outsourcing and Technology Transactions and in *Super Lawyers* as a New York Metro Rising Star. *Chambers* notes Mr. Angel “really knows the subject matter” and describes him as “smart and entrepreneurial” and a “superlative lawyer, very thoughtful and user-friendly.”

In the technology transactions area, Mr. Angel focuses on the development, acquisition, licensing and exploitation of intellectual property. He has substantial experience in patent licensing and cross-licensing agreements, the development and licensing of software, technology development and collaboration arrangements, content licensing and trademark licensing and co-branding agreements. He also regularly advises clients on intellectual property and information technology issues in connection with corporate transactions, including private equity representations, mergers and acquisitions, leveraged buy-outs and distressed lending. His experience includes negotiating and documenting intellectual property and information technology representations and warranties, complex transition services agreements, transitional trademark licensing arrangements and technology-related joint ventures and strategic alliances.

In strategic sourcing and commercial transactions area, Mr. Angel focuses on representing clients on legal and business issues relating to complex international outsourcing transactions, including structuring, negotiating and documenting information technology and business process outsourcing transactions. His information technology experience includes the outsourcing of numerous IT functions, including infrastructure, applications development and maintenance, end-user computing, help desk, desktop and network operations and his business process outsourcing experience includes the outsourcing of middle and back office financial services processes, facility management functions, insurance claims processing, human resources, payroll processing, finance and accounting functions and procurement. Mr. Angel also regularly represents clients on general commercial contracting arrangements, including supply and distribution agreements, co-packing arrangements, manufacturing agreements and servicing arrangements.

Mr. Angel received his Bachelor of Chemical Engineering from Villanova University in 1995 and his Juris Doctor, *cum laude*, from Tulane University School of Law in 2003 where he was the editor-in-chief of the *International and Comparative Law Journal*. In 2002, Mr. Angel served as a judicial extern for Judge Jay C. Zainey at the United States District Court for the Eastern District of Louisiana. He has been a member of the New York Bar since 2004 and the United States District Court for the Southern District of New York since 2005. Mr. Angel is currently in the third year of a three-year rotation as a member of the Trademarks and Unfair Competition Committee at the Association of the Bar of the City of New York and is a member of the Intellectual Property Committee at the American Bar Association.

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Stephen I. Glover is a partner in the Washington, D.C. office of Gibson, Dunn & Crutcher who has served as Co-Chair of the firm’s Global Mergers and Acquisitions Practice. Mr. Glover has an extensive practice representing public and private companies in complex mergers and acquisitions, joint ventures, equity and debt offerings and corporate governance matters. His clients include large public corporations, emerging growth companies and middle market companies in a wide range of industries. He also advises private equity firms, individual investors and others.

Mr. Glover was named the 2018 Washington, D.C. M&A Lawyer of the Year by *The Best Lawyers in America*[®] and has been ranked in the top tier of corporate transactions attorneys in Washington, D.C. for the past fifteen years (2005 – 2020) by *Chambers USA America’s Leading Business Lawyers*. He has also been selected by *Chambers Global* for the past five years as a top lawyer for USA Corporate/M&A. Chambers has singled out Mr. Glover as the only “Star” corporate lawyer in the District of Columbia. In 2018, he was recognized by BTI Consulting as a BTI Client Service All-Star MVP for making the Client Service All-Star list in four consecutive years.

Mr. Glover is the author or co-author of several books, including *M&A Practice Guide* (revised 2019); *Business Separation Transactions: Spin-Offs, Subsidiary IPOs and Tracking Stock* (revised 2019); and *Partnerships, Joint Ventures and Strategic Alliances* (revised 2019). He has written more than 60 articles and speaks frequently on corporate and securities law issues.

Mr. Glover has served as a member of the DC Bar Board of Governors, and as Co-Chair of the Steering Committee for the D.C. Bar’s Corporation, Finance and Securities Law Section. He is a member of the advisory board of BNA’s *Mergers & Acquisitions Law Report* and a member of the editorial board of *The M&A Lawyer*. He has served as D.C. representative to the New York Tribar Opinion Committee. Mr. Glover has also served as an Adjunct Professor at the Georgetown University Law Center.

Mr. Glover served as a law clerk to Justice Thurgood Marshall in the United States Supreme Court from 1981 to 1982 and to J. Skelly Wright, Chief Judge of the U.S. Court of Appeals for the District of Columbia Circuit from 1980 to 1981. He was the DC Bar Pro Bono Lawyer of the Year for 2004.

Mr. Glover earned his law degree *cum laude* in 1980 from Harvard Law School, where he was Managing Editor of the Harvard Law Review. He received his undergraduate degree *summa cum laude* from Amherst College.

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Sae Muzumdar is a partner in the New York office of Gibson, Dunn & Crutcher and Co-Chair of the firm’s Mergers and Acquisitions Practice Group. Ms. Muzumdar is a corporate transactional lawyer whose practice includes representing both strategic companies and private equity clients (including their portfolio companies) in connection with all aspects of their domestic and cross-border M&A activities and general corporate counseling. She has significant experience with acquisitions and divestitures of public and private entities (including both negotiated transactions and contested takeovers), venture capital investments, proxy contests, tender and exchange offers, recapitalizations, leveraged buyouts, spinoffs, carveouts, joint ventures and other complex corporate transactions. In addition, Ms. Muzumdar has represented a number of major investment banks as financial advisors in M&A transactions and financial institutions in connection with their investment activities.

Ms. Muzumdar’s corporate clients include Clorox, GE, Hologic, Kraft Heinz, Merck, News Corp., PepsiCo and Xylem, among others. Ms. Muzumdar’s private equity investor clients include Investcorp, J.H. Whitney and Tengram Capital, among others. Ms. Muzumdar’s investment bank clients include Centerview, Evercore, Goldman Sachs, Guggenheim Securities, Lazard, PJT Partners and UBS, among others.

Ms. Muzumdar has been recognized as a leading corporate attorney by *The Best Lawyers in America*®, as well as a “Rising Star” in M&A by the *International Financial Law Review*, *New York Law Journal* and *Law360*. She was named “Corporate Rising Star Attorney of the Year” by Euromoney Legal Media Group at its 2020 Women in Business Law Awards.

Ms. Muzumdar received her Juris Doctor, *magna cum laude*, in 2008 from the University of Michigan Law School, where she was elected to the Order of the Coif. She received her Bachelor of Arts degree from McGill University in 2005. Ms. Muzumdar is a member of the firm-wide Associates Committee, Lateral Partner Committee, Professional Development Committee and an active member of the Diversity Committee. Ms. Muzumdar also helps teach a mergers and acquisitions simulation course at New York University School of Law.

Ms. Muzumdar is admitted to practice in the State of New York.

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Ben Aylor is a core member of Boston Consulting Group's Health Care and Operations practice areas. He is BCG's global topic leader on network strategy for pharmaceutical manufacturing and has extensive experience with both strategy and operations projects in the pharmaceuticals industry, including biopharma network designs, operations transformations, make/buy analyses, and sourcing strategies.

Ben's current focus is on helping clients build their capabilities in new areas—such as digital supply chain—and meet the challenges of major change efforts including post-merger integrations and broad transformations. Ben has led both overall corporate PMI programs and the manufacturing aspects of PMIs.

Before joining the firm, Ben worked at Arthur Andersen Business Consulting.

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Since joining Boston Consulting Group in January 2015, Hob Brooks has focused almost exclusively on health care operations and supply chain engagements, working with large pharmaceutical, medtech, and consumer health care clients. In addition to his client work, Hob is actively involved in recruiting and was previously the recruiting director for the Philadelphia office.

Hob advises biopharmaceutical and medtech companies on complex large-scale transformation programs and pre-/post-merger transaction planning, execution, and integration. He is also a trustee and member of the board for the Pennsylvania Ballet.

Prior to joining BCG, Hob worked as Senior Director of Business Development at Wolters Kluwer Health, where he focused on identifying and negotiating key strategic partnerships for the business and assisted with creating a pipeline for corporate development opportunities. Before Wolters Kluwer, Hob worked in sales and sales management roles with SAGE Publications and Thomson Reuters.