What path will you navigate to carve-out sale success?

Road map part 1: Getting the deal signed in six months

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Building a better working world

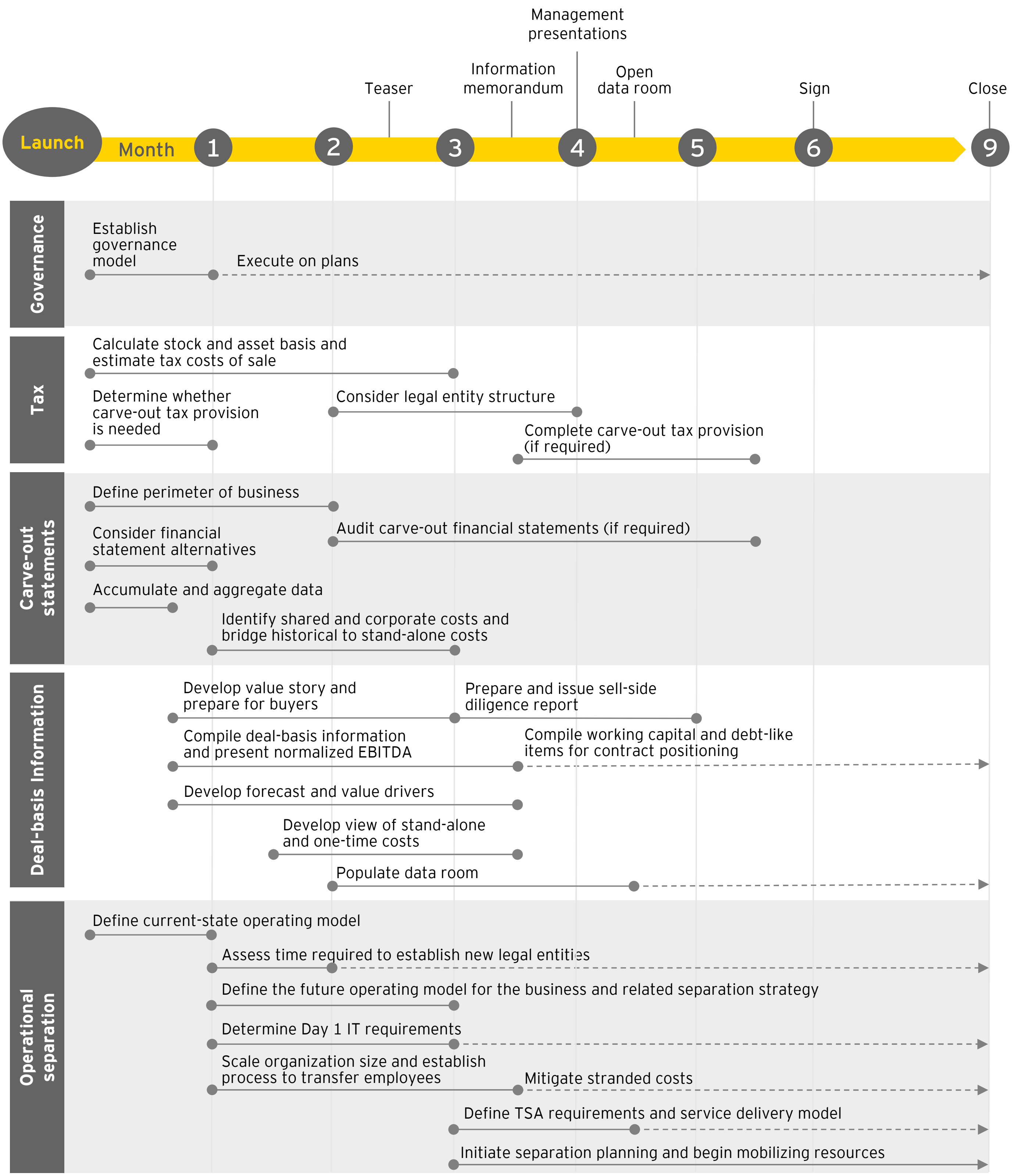
Are you considering selling a business based on a strategic portfolio review?

What would it take to sign the deal in just six months?

Successful sellers understand that carving out a business is often more complex than acquiring one. Selling a carve-out requires a greater level of planning, effort and urgency — but thinking like a buyer helps you control and expedite the process.

Here we highlight the critical steps to getting a deal signed in six months. First, company leadership needs to mobilize a multidisciplinary team and establish a governance structure that defines the transaction timeline, goals, roles and responsibilities. This team represents the entire enterprise, including tax, finance, supply chain, information technology, human resources, legal and communications. With the governance structure in place, the teams must prioritize high-impact tax, financial and operational separation work streams.

Our EY Divestiture Advisory Services teams can help focus your efforts to accelerate transaction closing, minimize business disruptions and protect value.



Management presentations
Teaser
Information memorandum
Open data room
Sign
Close
Launch
Month
1
2
3
4
5
6
9
Governance
Establish governance model
Execute on plans
Tax
Calculate stock and asset basis and estimate tax costs of sale
Determine whether carve-out tax provision is needed
Consider legal entity structure
Complete carve-out tax provision (if required)
Carve-out statements
Define perimeter of business
Consider financial statement alternatives
Audit carve-out financial statements (if required)
Accumulate and aggregate data
Identify shared and corporate costs and bridge historical to stand-alone costs
Deal-basis Information
Develop value story and prepare for buyers
Prepare and issue sell-side diligence report
Compile deal-basis information and present normalized EBITDA
Compile working capital and debt-like items for contract positioning
Develop forecast and value drivers
Develop view of stand-alone and one-time costs
Populate data room
Operational separation
Define current-state operating model
Assess time required to establish new legal entities
Define the future operating model for the business and related separation strategy
Determine Day 1 IT requirements
Scale organization size and establish process to transfer employees
Mitigate stranded costs
Define TSA requirements and service delivery model
Initiate separation planning and begin mobilizing resources

Improving carve-out sales

Governance

Establish a divestiture governance model

- A strong governance structure can mitigate divestiture risks – it helps identify priorities and manage key deadlines, interdependencies, resource constraints, decision-making and stakeholder expectations.
- An executive steering committee, functional separation leaders and an internal and external communication strategy help define roles and responsibilities and facilitate execution.

Tax

1. **Determine which entities will be sold as stock vs. assets and calculate tax gain or loss**
   - An anticipated tax bill may drive a "go or no-go" decision and help focus on how to maximize after-tax proceeds.
   - Stock vs. assets structure affects tax indemnities, after-tax proceeds and the buyer's ability to fund debt repayment, distributions to shareholders or other business needs.
2. **Consider a legal entity structure that can help maximize value to a buyer and reduce tax on sale and repatriation of proceeds**

   Strategies that appropriately reduce future cash taxes and effective tax rate may increase valuation.
3. **Anticipate whether a tax provision for full financial statements will be needed**

   A tax provision is required for audited carve-out financial statements; however, it is not required for abbreviated financial statements.

Carve-out financial statements

1. **Define perimeter of the business and how it might be packaged (e.g., sold as a whole or split and offered to multiple buyers) and identify components that may later be included or excluded**

   This affects all other carve-out work streams.

2. **Consider financial statement alternatives (full, abbreviated or deal-basis and audit requirement)**
   - Audited financials require significant effort from corporate and field personnel, along with knowledge of carve-out accounting rules.
   - Providing only unaudited deal-basis financials may affect the buyer pool and valuation (e.g., if the buyer needs audited financials for financing purposes or regulatory purposes).

3. **Accumulate and aggregate data (financial reporting model)**
   - Sellers should use a model to aggregate data and post adjustments to prepare carve-out financial statements.
   - A trail of historical data and carve-out adjustments facilitates the audit, diligence and reporting of discontinued operations (if applicable).

4. **Identify shared and corporate costs and bridge historical to stand-alone cost estimates**
   - Direct and indirect costs must be reflected in historical carve-out financials; deal terms do not dictate accounting treatment.
   - Allocations in carve-out financials are different from those in deal-basis financials; insufficient preparation can lead to delays.

Deal-basis information

1. **Develop value story and tailored materials and prepare for buyers**
   - Value story linking historical and forecasted operating results, and market assessment, supports consistent messaging and facilitates speed to sign.
   - Management preparedness instills buyer confidence and helps control the discussion of the business being sold.
   - A comprehensive and self-service data room reduces interactions with buyer advisors and provides time to manage the business and discuss the salient issues with the buyer.

2. **Compile deal-basis information and normalized EBITDA**

   Buyers generally index purchase price on an EBITDA multiple.

3. **Develop forecast and value drivers**

   Linking historical with projected results improves credibility.

4. **Develop a view of stand-alone and one-time costs**
   - Buyers can make better-informed decisions when they understand a company's operating model, potential synergies and stand-alone costs.
   - Sellers can also protect or enhance value by controlling buyer assumptions.

5. **Prepare sell-side diligence report**

   During a complex auction process, a well-prepared and comprehensive seller diligence report may help enhance competition and expedite buyer diligence.

Improving carve-out sales

Operational separation

1. **Define current-state operating model**

   Understanding current operations helps avoid surprises that could decrease deal value or delay closing.

2. **Assess time required to establish new legal entities**

   - Requirements to establish new legal entities vary by jurisdiction and industry and can take over a year to complete.
   - Failure to act expediently can delay establishing bank accounts, contracting with vendors, configuring systems, establishing processes, selling product and other downstream activities, and can delay (or stagger) closing.

3. **Define the future operating model for the business and related separation strategy**

   - An optimized future operating model can enhance deal value.
   - A credible separation strategy shows buyers that the business can be separated without loss of value.

4. **Determine IT requirements to operationalize new legal entities, segregate access and data, address name changes and enable separate financial reporting**

   IT is often the most entangled functional area and the one that requires the most lead time and it is typically the most expensive to separate. Starting early can reduce the time between sign and close, reduce complexity and cost and reduce Transitional Service Agreement (TSA) scope.

5. **Right-size the organization being transferred and establish process to transfer employees**

   The existing organization model is often not optimal for the future state of a carved-out business that will operate independently or be integrated into a buyer's operations — an appropriate size optimizes costs.

6. **Define TSA requirements and service delivery model**

   This helps buyers understand complexity and cost to operate on Day 1 and to exit TSAs; a proactive approach also helps sellers identify and remediate stranded costs.

7. **Initiate separation planning and begin mobilizing resources**

   - Most separation activities occur between signing and closing, but planning and implementing early can shorten this timeframe and help reduce the need for TSAs.
   - Finance, human resources, supply chain and IT functions are typically the most affected, requiring significant planning and resources to successfully separate.
   - Legal entity separation and stand-up activities impact most functions, so the seller must integrate interdependencies into planning to reduce disruptions.

Summary

Below we suggest some guiding principles as you navigate the critical steps of a carve-out sale transaction.

- **Gain leadership commitment** — Sellers need properly resourced teams, clear roles and responsibilities, and a communication strategy that align key stakeholders.
- **Make the management team of the carved-out entity feel like shareholders of the divested business** — A credible management team decreases risk of value leakage.
- **Maintain a buyer mindset** — When you understand your buyer pool, you can better tailor information to their needs. Providing compelling and credible information helps maximize value and shorten the transaction life cycle.
- **Understand value, speed and risk tradeoffs** — You have to know what you're willing to sacrifice if you decide not to commit capital or resources to specific tasks.
- **Understand operational separation challenges** — Don't underestimate the lead time or resources needed to separate your business.

Keeping these principles top-of-mind as you manage the four critical work streams will help you control the process and drive toward a signed agreement within six months.

Guiding principles

- Gain leadership commitment
- Make management team of carved-out entity feel like key stakeholders of the divested business
- Maintain a buyer mindset
- Understand value, speed and risk trade-offs
- Understand operational challenges

Governance
Maintain deadlines and mitigate risks

Tax
Increase after-tax proceeds and assess impact on operational separation

Carve-out financial statements
Expedite the audit and reporting process

Deal-basis information
Create a strong and credible value story

Operational separation
Define changes to operating model and their impact on historic and stand-alone entity cost structure

Enhance operating model (people, processes and systems)

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