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

Road map part 2: Sign to close

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Congratulations; the deal is signed. Now another phase of heavy lifting begins. How do you successfully close your carve-out sale in only three months without eroding value or destroying the deal?

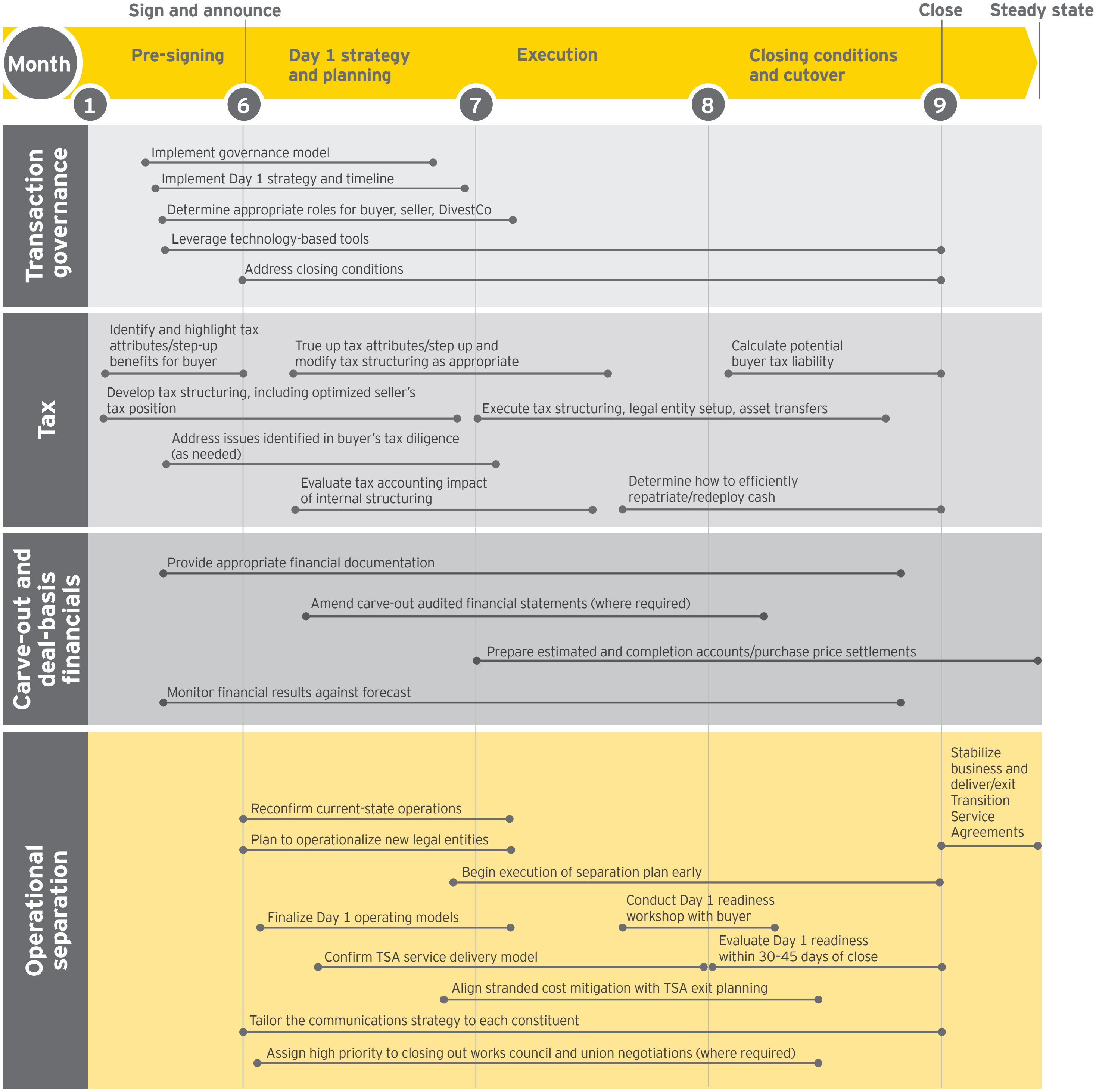
Once the carve-out sale agreement is signed, the focus shifts to separating the business from the parent company and transitioning to the buyer — without disrupting operations. Planning performed prior to deal-signing pays dividends, as attention turns to the following separation priorities:

- **Implement separation governance.** While project management is a component of governance, effective governance is ultimately about decision-making. Clearly defined decision-making rights and guiding principles focused on prioritizing separation requirements are critical when working with a buyer to preserve value and transition as much of the business as possible pre-close.
- **Finalize the Day 1 operating model.** Before the business can be separated, key processes at each impacted location must be understood at a detailed level. Different factors can have significant closing environment trade-offs and implications that consistently challenge experienced management teams. For example, buyer readiness constraints and market authorization requirements often necessitate developing an interim operating model for Day 1 with the buyer.
- **Finalize workarounds for long-lead-time separation activities.** These next three months are rarely sufficient time to finalize separation of IT systems, form new legal entities that are ready to conduct business and address all regulatory requirements. Creative workarounds get the deal closed.

Read this road map for details on the most critical considerations.

Carve-out sign-to-close road map timeline

Closing the deal within three months



Closing carve-out sales

Transaction governance

Implement governance model

- Organize a kickoff with buyer to align on guiding principles, Day 1 strategy and governance model
- Understand interdependencies across work streams to avoid issues that could delay or derail closing
- Develop a separation team of RemainCo/seller owners and DivestCo members to develop plans and identify TSA requirements jointly

Determine the appropriate roles for DivestCo, seller and buyer

- Seller is responsible for maximizing shareholder value and should lead each separation work stream
- DivestCo employees should drive execution and knowledge transfer
- Buyer should assign sufficient resources to integrate and support operations

Implement Day 1 strategy and timeline

- Review key drivers: desired closing timeline, capabilities, separation complexity and regulatory constraints
- Align with buyer on strategy by function and TSA needs in order to avoid gaps
- Understand lead time to address closing conditions, as well as responsibility

Leverage technology-based tools

- Use web-enabled tools to streamline and automate status reporting
- Get a jump-start with EY Divestiture playbook, providing a methodology and customizable tools

Address closing conditions

- Review multiple payments, foreign currencies and regulatory restrictions that complicate closing funds flow
- Develop creative workarounds for long-lead-time activities in order to close the deal

Tax

Address issues identified during buyer's confirmatory tax diligence (as needed)

- Provide for timely closing
- Enable refinement of indemnity language and threshold amount in sale and purchase agreement
- Consider warranty and indemnity insurance process and anticipate underwriter discussions

Identify, highlight and true up tax attributes and modify tax structuring as appropriate

Evaluate tax accounting impact of any internal structuring

- Changes to deferred tax assets/liabilities may impact seller/RemainCo's effective tax rate

Execute tax structuring, legal entity setup and/or asset transfers

- Create new legal entities and transfer/retitle of assets, which is generally complicated and time-consuming
- Manage tax rollovers, value-added tax and transfer taxes

Determine how to efficiently repatriate/redeploy cash

- Consider impact of permanent reinvestment, applicable withholding taxes and requirements for treaty benefits
- Verify that transaction documentation supports intended structuring outcomes

Calculate potential buyer tax liability/filings

- Transfer tax may be split liabilities between buyer and seller
- Understand buyer/seller responsibilities to file documentation and interact with tax authorities

Carve-out and deal-basis financials

Amend carve-out audited financial statements

- Continue to bridge audited financial statements to deal-basis financial statements to reflect ongoing perimeter changes and assess impact on deal value
- Consider the buyer's need for updated carve-out audited financial statements for financing or regulatory filings; audit updates take time and can severely impact deal timing
- Assess impact of new accounting pronouncements and their applicability — retrospective application may require significant time and effort from the seller and the auditors

Analyze balance sheet and plan for post-closing activity to avoid surprises and delays

- Continue to review monthly or quarterly working capital and other balance sheet accounts to avoid delays related to the closing mechanism
- Monitor net debt and off-balance sheet items so that impacts are considered from a value perspective
- Identify significant variations in completion accounts/working capital settlement amounts as they may result in disputes with buyer

Monitor financial results against forecast to avoid disputes or value loss

- Analyze monthly or at least quarterly results so that the seller is prepared to explain any discrepancies and/or manage purchase price payment expectations with seller/buyer at closing
- Monitor synergy realization to provide alignment with value story

Provide appropriate level of financial documentation in data room

- Assess data room and remove items that are no longer relevant to avoid redundant questions

Plan for closing/post-closing

- Monitor and optimize relevant cash items (net working capital and net debt), including any pre-completion dividend payments
- Plan for completion accounting post-closing

Operational separation

Reconfirm current-state operations

- Review the current-state operations immediately after signing, as in-scope assets may change

Execute plan to operationalize new legal entities

- Review plan for long-lead-time countries due to transaction structure requirements (e.g., stock vs. asset sale, insufficient buyer readiness, enterprise resource planning (ERP) systems may need to be configured to support the new legal entity)
- Get vendors (e.g., financial institutions and payroll providers) prepared for the timeline

Finalize Day 1 operating models to close the deal

- Consider workarounds, whereby the seller continues to operate portions of the business on behalf of the buyer
- Drive Day 1 operating model development so that the deal closes and transition support is minimized

Focus on execution of separation plan to shorten time to close and minimize workarounds

- Address critical functions requiring significant resources to support:
  - Interim reporting (e.g., helping the buyer close the books Day 1)
  - ERP systems that often require logical and physical separation of commingled data and systems
  - Marketing products: managing product registration lead times
- Understand competing seller strategic initiatives and potential impact on separation activities
- Enable buyer readiness to avoid closing delays (e.g., systems capabilities, presence within existing markets, weight of speed (TSAs) vs. value (degree of separation by close))
- Focus on Day 1 "must-haves" and challenge buyer's optimization efforts (e.g., emphasizing critical functions such as order-to-cash)

Closing carve-out sales

Operational separation (continued)

Focus on execution of separation plan to shorten time to close and minimize workarounds (continued)

- Anticipate currency controls and banking rules to avoid stranded cash
- Consider customer and supplier contracts, including property leases, which may require notifications or a lengthy consent process

Confirm TSA service delivery model

- Finalize the TSA schedules, which document how post-closing services will be delivered, disputed and exited

Align stranded cost mitigation with TSA exit planning

- Finalize requirements to support buyer with services under a TSA, which may restrict ability to mitigate stranded costs
- Set ambitious budget targets to hold business unit leaders accountable for mitigating stranded costs

Assign a high priority to closing out works council and union negotiations (as needed/where required)

- Review changes in employment terms and conditions and legal entities that drive employee consultation requirements
- Close out negotiations on transfer requirements to avoid closing delays

Tailor the communications strategy to each constituent

- Contact key customers and suppliers as soon as the deal is announced
- Maintain dialogue with customers and suppliers on changes to how they order or pay to minimize disruptions and implement a dispute resolution process
- Implement an employee communications strategy addressing transition arrangements, time off, compensation, year-end processes, and changes to health or pension benefits

Evaluate Day 1 readiness within 30-45 days of close to allow adequate time to change course

- Enable progress monitoring, risk identification and timely issue resolution
- Focus on interdependencies, such as the impact of a system blackout period during cutover
- Conduct Day 1 readiness workshop as a joint session to gain full alignment that closing is actually ready to happen from the perspective of both the seller and buyer

Operationalizing a legal entity

Functional separation considerations:

Technology and data readiness

- Determine IT requirements to operationalize new legal entities, segregate access to systems and data, address name changes and enable separate financial reporting
- Refine a clear master data segregation strategy and IT governance structure

Supply chain, manufacturing and regulatory

- Confirm registrations, licenses and financial guarantees that must be addressed by closing and potential impacts to the supply chain
- Develop agency/distributor arrangements or other workarounds with the buyer to close the deal based on buyer capabilities and seller IT, regulatory and finance functional constraints
- Negotiate long-term supply or transitional arrangements to maintain ongoing manufacturing and drive desired behaviors
- Review opportunities to rationalize the operating footprint or simplify the operating model

Human resources matters

- Implement an employee engagement strategy to help stakeholders through the transition
- Consider RemainCo retention programs for areas with significant shared resources
- Set up payroll and benefits, which may have long lead times due to data privacy/integrity, vendor availability, notice and consent periods
- Review statutory pension requirements and terms for in-scope employees to evaluate implications on the sale price, seller's financial statements and cash flow

Finance

- Provide continuity of systems and key business processes (e.g., order-to-cash, procure-to-pay)
- Settle intercompany balances
- Focus on Day 1, Month 1 and Quarter 1 reporting

Summary

Below, we suggest some guiding principles to drive toward a successful closing in three months:

- **Governance is more than project management** — Timely decision-making is critical to drive alignment with the buyer on Day 1 requirements, or issues at closing could result in a distracted management team or lost value. Teams should appoint an executive that will remain with the seller to lead the project management office (PMO) and leverage leading practice tools in order to avoid delays.
- **Expect allegiances to shift** — The divested unit management team's allegiance will pass to the buyer likely before close, so have appropriate governance to confirm those aligned to DivestCo are not acting in a manner inappropriate to the seller.
- **Define the operating model needed to deliver services to the buyer** — Services are contractually agreed to in TSA/commercial agreements, but failing to define the service delivery model can result in disruptions and disputes, which could distract management from running the existing business.
- **Prioritize long-lead-time activities** — Activities such as operationalizing new legal entities, consultations with works councils and unions, obtaining regulatory approvals and receiving support needed from vendors can take longer than expected and may delay closing for months if not appropriately addressed.
- **Periodically track performance against buyer expectations** — Keep a current view of expected working capital and any other post-closing-related mechanisms to appropriately prepare for value impacts and post-closing negotiations.
- **Enable consistent involvement of tax** — This supports maintaining value for the seller and efficient transfer to the buyer. This also includes a separate tax PMO to safeguard tax benefits, reduce tax costs and meet timeline.

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