Attributes of spin-offs, carve-outs or divestitures

Definition

- Seller divests a "non-core" division; a distinctly different product / segment or capability to a new "control" owner
- Assets may be integrated into an existing strategic buyer; or contributed to a Newco or JV
- Equity Carve-out (partial spin-off) where parent retains control but sells a stake in a recapitalized division to other investors, typically through IPO

Characteristics

- Includes elements of acquisitions & start-up
- Typically dependent on Seller for delivery of key services for transition period
- May or may not have financial statements and operational metrics for the asset(s) / division being spun-off
- Unique change management issues and perceptions

Priority Issues

- Lack of Seller support is #1 failure factor
- Failure to achieve adequate independence is #2 failure factor
- Must carefully define Transition Services Agreement(s)
- Essential to get systems, functional and business process assessment right
- Talent, change and "me issues" are paramount
- Must quickly align on strategy, vision and high-performance cultural attributes

Example: Health care products company, Covidien PLC spun off its pharmaceutical business into a new publicly traded company, Mallinckrodt PLC, effective June 28, 2013 to enable each entity to focus more effectively on their core segment and growth strategies.

Failure factor #1:

- **The Seller fails to provide the critical strategic, organizational, operational, financial or legal transition support required for launch and success**

Four Traps:

- Crown Jewel Trap: too close to remaining core business

- Piggy Bank Trap: short-term tactical vs. long-term strategic

- One-Legged Stool Trap: lacks key components needed to ultimately success

- Umbilical Cord Trap: Seller's continued interference or failure to cede true operating control (Failure factor #2)

Source: Spinning Out a Star, Harvard Business Review

Frequent spin-off, carve-out & divestiture mistakes

- **Culture**
  - Failure to define the vision and ensure alignment with high-performance cultural attributes needed in the new environment
- **Organization design and strategy**
  - Use of a “clone & go” approach vs. adapting organizational thinking, policies, practices and systems to Newco business and strategic requirements. Ex: incentive design and performance expectations
- **Talent**
  - Failure to recruit the best of both legacy organization and new-hires
  - Seller “cherry picks” key talent prior to spin-out
- **Dependency syndrome**
  - Entangled governance, infrastructure and operations prevent true “stand-alone” capabilities
- **Change resistance**
  - Potentially greater change resistance in spin-outs than typical M&A
  - Harder to explain; perceptions of rejection / betrayal – “they eliminated an unwanted asset”
  - Uncharted career waters – increased uncertainty and risk
  - Some employees may perceive public-to-private spin-outs as less desirable due to diminished transparency / compliance and loss of equity participation opportunities