

14th Annual Mergers and Acquisitions Institute

More Cake: Advanced Issues in Carve-Outs and Divestitures

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Agenda

- Deal Structure
- Due Diligence
- IP Matters
- HR Matters
- Successor Liability
- Ancillary Agreements /
Non-Compete and Non-Solicit
- Transition Services
- Considerations for
Multi-Jurisdictional Carve-Outs
- Defining the Sale
- Third Party Approvals

Deal Structure

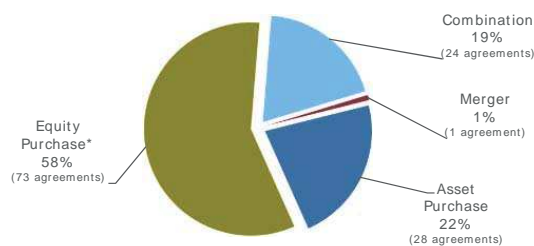
- First step in a carve-out transaction is identifying the assets and liabilities to be transferred to Buyer and retained by Seller
- Next, determine optimal deal structure: stock sale vs. asset sale. Two important considerations: tax and assumption of liabilities
 - Tax: Parties must evaluate whether stock or asset sale is most tax efficient
 - Impact on buyer and seller may differ
 - Assumption of Liabilities: Buyer should be aware how deal structure impacts the liabilities it assumes post-transaction
 - Stock Sale: Liabilities of the carved-out business generally pass to Buyer by operation of law (may be able to seek protection from certain liabilities through indemnification)
 - Asset Sale: Buyer assumes only those liabilities it specifically assumes as part of the negotiated asset purchase agreement
 - Note: Under certain state, federal and international law, certain liabilities may pass to Buyer or be retained by Seller even if parties have allocated liabilities differently in purchase agreement

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Deal Structure

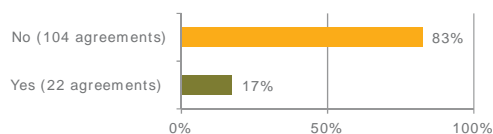
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Structure of the Transaction



* One agreement included as an equity purchase contains an asset purchase component, but is excluded from the subset "involving an asset purchase" because it is not primarily an asset purchase and does not contain the common features of an asset purchase.
Ten agreements that involve an equity purchase expressly provide for a pre-closing reorganization whereby assets of the carved-out business are contributed to a subsidiary of the Seller that is acquired by the Buyer.

Simultaneous Sign/ Close?*



** Some simultaneous sign and close agreements include attributes that are typical for agreements that do not contain a simultaneous sign and close (e.g., closing conditions and termination provisions). Therefore, throughout this Study we have included agreements with a simultaneous sign and close structure in subsets where these agreements contain the applicable features being analyzed.

Practice Pointer:

41% of the agreements (52 agreements) are structured as an asset purchase or combination of asset and equity purchase. Certain logistical issues arise when transactions are structured to include an asset purchase.

These logistical issues may include:
(i) commingled contracts (contracts of the Seller that cover both the carved-out business being sold and other businesses that will be retained by the Seller after completion of the carveout); (ii) third party consents may be necessary to assign contracts; (iii) the Seller's books and records are frequently maintained on a consolidated basis, thus making it difficult to transfer separate records for the carved-out business being sold; (iv) additional documents are often required in order to effectuate an asset transfer such as bills of sale, assignment and assumption agreements and other legal documents that may be required to be delivered and/or filed in order to effect and/or record transfers of certain assets, such as real property or intellectual property; and (v) the need to create, and in some cases license to, legal entities to receive the assets (which may require significant time and effort in some foreign jurisdictions).

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Due Diligence

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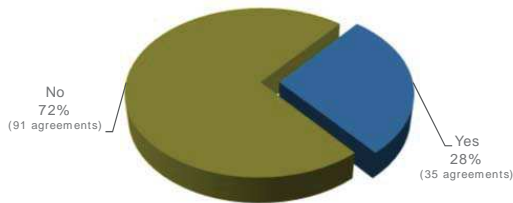
- Legal Due Diligence
 - Due to nature of carve-out transaction, Buyer must be prepared for heightened due diligence to identify assets / liabilities that should be transferred to Buyer or retained by Seller
 - Commingled contracts
 - Contracts covering both transferred and retained businesses
 - How do parties want to treat these contracts?
 - If parties want to unwind, which party is responsible and what should be the applicable efforts standard?
 - How will contracts be unwound? Is carved-out business released from contract, or is commingled contract split into two?
 - If required, which party will be responsible for acquiring necessary consents?

Due Diligence

Continued

Commingled contracts are contracts that cover the carved-out business and all or part of the business to be retained by the Seller. Unwinding refers to the situation in which the carved-out business is released from the commingled contract, or the commingled contract is split into separate contracts (whether by novation, partial assignment or amendment, or some combination thereof).

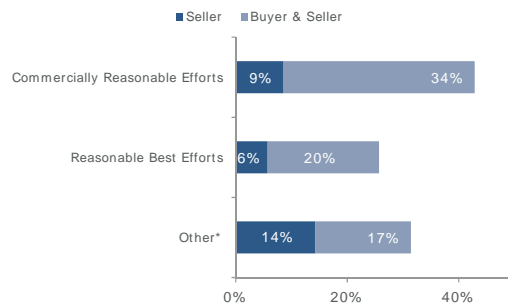
Commingled Contracts to Be Unwound



35 agreements (28%) expressly provide for the unwinding of commingled contracts. 14 of these agreements provide for unwinding as both a pre- and post- closing covenant, 17 solely as a pre-closing covenant and three solely as a post-closing covenant. One agreement provides the covenant for unwinding of commingled contracts on a schedule not publicly available. Of those agreements that include an unwinding provision, most designate both the Buyer and the Seller as responsible for effectuating the unwinding.

Standard for Unwinding Based on Which Party is Responsible for Unwinding

(subset: 35 agreements providing for unwinding of commingled contracts)



- * "Other" includes:
- (1) Bifurcated pre-closing responsibility to the Seller on a commercially reasonable efforts basis and post-closing responsibility to the Buyer on a reasonable efforts basis.
 - (1) The Seller with an "obligation of result" (i.e., must cause the termination).
 - (2) The Seller must do all things/actions necessary.
 - (1) The Seller bears responsibility, but there is no standard provided.
 - (1) The Seller bears responsibility, but standard is provided on schedule.
 - (1) Both bear responsibility, but there is no standard provided.
 - (4) Both bear responsibility and must cooperate with each other.

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