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5x5 series: Insights and actions

Be a prepared seller: Accounting and tax considerations for divestiture planning

In the current inflationary environment, divestiture activity—including carve-outs and spin-offs—is increasing as many organizations seek to maintain flexibility and resiliency in the midst of economic uncertainty. While deal volume in the divestiture market has declined from 2021, there is still strong demand in the marketplace and lack of preparation can cause timeline delays, loss of value, and additional layers of disruption. Appropriate forethought and attention throughout the divestiture process can help organizations to become prepared sellers and realize more successful sell-side outcomes.

5 insights you should know		*5 actions you can take*
Define the transaction perimeter – A clearly defined and set transaction perimeter is essential when divesting a portion of the organization as it will drive deal economics, inform the content of the financial information shared in the diligence process, and will be the basis for tax structuring activities.	1	Identify the assets, liabilities, and operations included within the transaction perimeter, including the legal entities subject to the transaction. A clearly defined perimeter can help the appropriate level of rigor and detail to be applied to the financial and tax information that will be shared in the diligence process and support audit activities (as required).
Identify entanglements – Be aware of operational and legal entity entanglements between the seller and asset to be divested. Discovering an entanglement late may result in an unnecessary transition service agreement (TSA), delay in closing, or even a change in transaction price.	2	Prepare a bottom-up review of business processes to identify specific entanglements. Assess the current state of the business and envision what's needed to operate independently on Day 1, starting even before the sale is being negotiated. Engage relevant individuals in the organization to evaluate what's required for the transition and reconfirm TSAs and any assumptions made pre-close.
Anticipate alternative divestiture scenarios – It's not uncommon for organizations to change their divestiture strategy (e.g., a spin-off becomes a sale or vice versa) to respond to stakeholder expectations or due to changes in an organization's overall M&A strategy. A prepared seller should be ready to pivot and anticipate other transactional alternatives.	3	Prepare diligence materials in a manner that supports a variety of exit scenarios. Establish "command and control" governance to quickly react and make decisions as alternative divestiture scenarios arise. As changes occur, close coordination with stakeholders across the organization is essential for them to understand how their workstream may be impacted.
Stay ahead of the due diligence process – Inaccurate or incomplete financial and tax information shared in the diligence process can result in increased scrutiny from the buyer, decrease confidence in management, and extend the sale process. Sellers can mitigate such repercussions by preparing fully developed diligence materials in advance.	4	Preparing a vendor due diligence report, a quality of earnings report, or a tax fact book can provide context on relevant financial information and key accounting and tax matters, provide more control over the sale process, improve the quality of information to be provided to buyers, and prepare management on due diligence findings to mitigate potential risks.
Consider the go-forward cost structure – As the organization transforms through the sale of assets or businesses, management should consider the operations and cost structure of the residual business, such as stranded costs, long-term supply impacts, and new tax planning considerations, in an effort to enhance and preserve deal value.	5	Develop a clear understanding of the structure of the residual business controlled by the seller post-divestiture. Perform a detailed bottom-up analysis early in the planning process to mitigate stranded costs as efficiently as possible and develop post-divestiture tax planning.

Connect with us

BRENDA CIAMPOLILLO
Managing Director
Deloitte & Touche LLP
bciampolillo@deloitte.com

CLIF MATHEWS
Partner
Deloitte & Touche LLP
clmathews@deloitte.com

DAVID OBERST
Partner
Deloitte & Touche LLP
doberst@deloitte.com

RYAN STECZ
Partner
Deloitte Tax LLP
rstecz@deloitte.com