Divestiture Management Office (DMO)

Achieving effective divestiture across the enterprise

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At a glance

Failure to capture deal value is rarely due to a flawed strategy; most often, it's a result of not executing the strategy in an effective and timely manner.

Converting divestiture strategy into detailed actions that align people, process, and systems with divestiture objectives requires an effective governance structure – a Divestiture Management Office.

A well designed and operating DMO will assist a divestiture to stay on course and sustain focus on the right activities at the right times.

Introduction

Transactions can be complex and difficult to execute, particularly divestiture transactions. Study after study shows that most divestitures fail to realize their expected value. Yet failure to capture divestiture value is rarely attributed to a flawed strategy. Rather, failure is most often a result of not identifying the opportunity to divest in a timely manner, or not executing the divestiture strategy with an effective approach.

Successful divestitures must happen quickly and systematically — the period of time between launching internal activities and deal close, and the initial period post close, are absolutely critical to maximizing divestiture value and optimizing remaining company value over the long-term. To succeed, a governance structure must be in place to align people, process, and systems with divestiture and separation objectives. This is the role of the Divestiture Management Office (DMO).

A DMO is the glue that holds a divestiture together. It is the nerve center of the effort. It serves as the central touch point for every function and individual involved, and it must be specifically designed to meet the needs of the deal it serves. A DMO staffed by experienced resources with a common timeline and methodology is necessary to ensure the divestiture stays on course and the individuals involved in the effort focus on the right activities at the right times.

The issues our clients face, the actions we help them take

At PwC, we understand the importance of getting divestiture fundamentals in place as quickly as possible. We support our clients by rapidly launching efforts to help achieve three primary objectives: increase deal value, realize a smooth transaction close, and minimize disruptions throughout the divestiture and separation process. Figure 1 illustrates the divestiture and separation process.

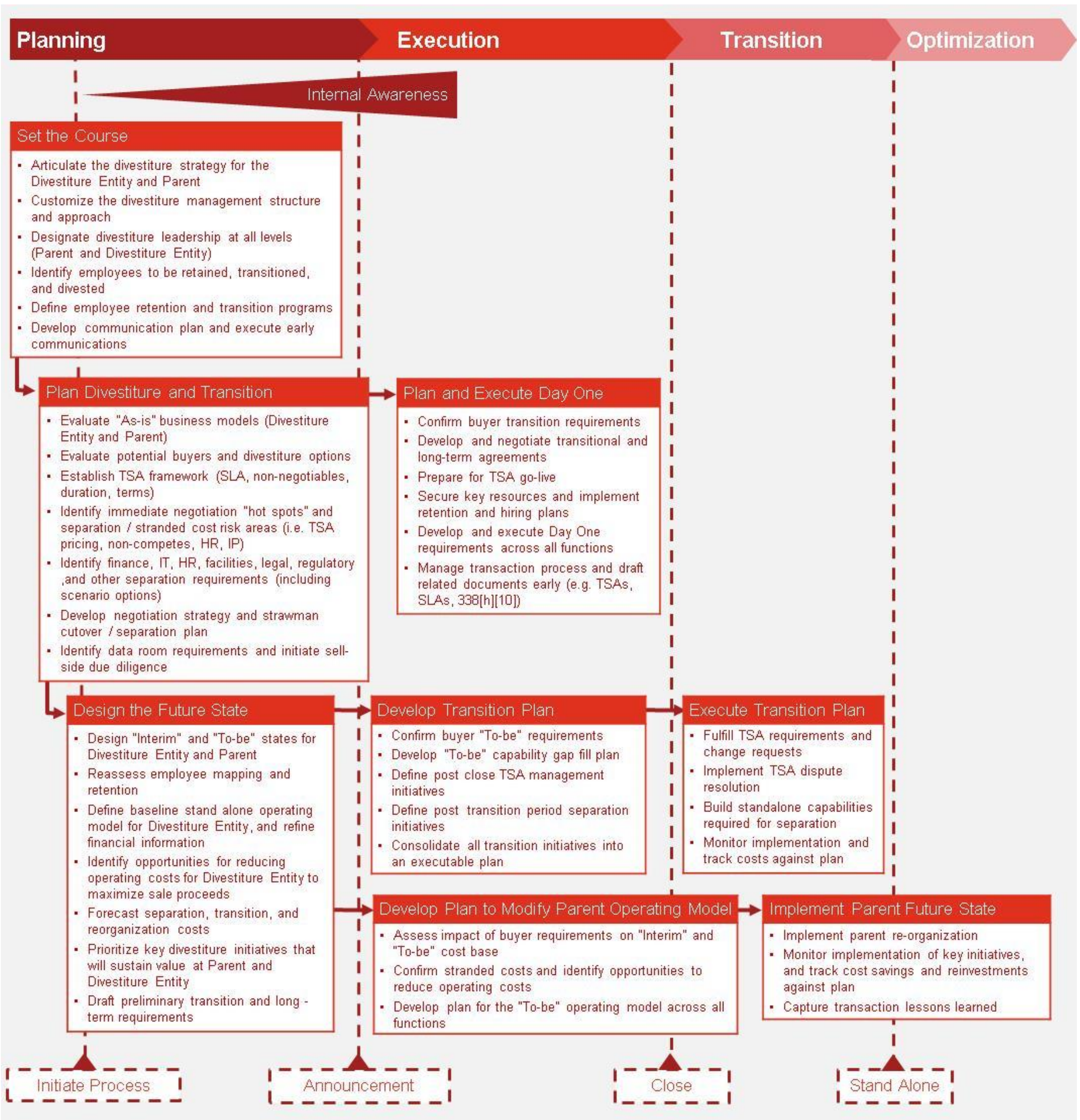

Figure 1 — The PwC divestiture and separation process follows a sequence of coordinated steps to focus people and capital on the right activities at the right times.

While a disciplined process is important for divestitures, the process must be flexible enough to adapt to each transaction's unique facts, circumstances, and evolving needs. The primary purpose of a DMO is to put in place the management structure, people, and processes that match the divestiture requirements in pursuit of capturing deal value. A DMO accomplishes this by:

- Defining the divestiture fundamentals, including the degree of separation and non-negotiables across functions and geographies
- Establishing a disciplined approach to coordinate the divestiture and separation activities across the organization
- Sequencing roll-out of the divestiture methodology and tools, including status reporting and dependency and issue management
- Identifying issues, decisions, and resource constraints, and escalating to management for resolution
- Launching key communications and the communication planning process

In larger divestitures with significant separation requirements, the DMO is also responsible for implementing centralized processes in complex areas. This requires the collection and analysis of information and input from multiple functions, such as Transition Service Agreement (TSA) development, stranded cost analysis, and implementation of the go-forward operating model and the resulting infrastructure reorganization.

Divestiture Management is more than just Project Management

Divestiture management is not just project management. While some elements of traditional project management are found within a Divestiture Management Office (DMO), a DMO is much more. All too often even the most seasoned of senior managers underestimate the complexity and duration of a divestiture transaction, particularly in large-scale cross-border transactions. A common mistake is made by assuming that typical project managers have the experience to manage the exponential complexity of divestitures. Typical project management often involves only a handful of workstreams within a single or limited number of functions. Scope is also typically limited and timeframes are generally well defined.

Divestiture management, on the other hand, is much more pervasive. It normally involves all aspects of the organization, has a fluid scope, and evolving timelines. Outside factors, such as buyers and capital markets, can significantly impact volume and duration of the divestiture activities, requiring the divestiture organization to remain flexible and adjust to shifting priorities and requirements over different phases of the divestiture. The level of executive support and oversight required is often much higher given the strategic nature of a transaction. Failure to recognize and address these factors early is the first warning sign of divestiture failure.

Set the course

A divestiture transaction, like other corporate change initiatives, is an excellent opportunity to set a new course — both operationally and across various support functions. Setting the course involves defining clear objectives and establishing clear leadership and role clarity throughout the transition.

Key areas for the Divestiture Management Office (DMO) to "*Set the Course*" include:

Establishing the Divestiture Organization

The divestiture organization is comprised of cross-functional teams responsible for executing the tactical divestiture and separation plans within the parent, the divestiture business unit, and each function. It is a team-based control structure that links divestiture strategy and leadership with task-level actions. The divestiture organization is best assembled once the overall divestiture strategy has been developed and translated into guiding principles that define the divestiture objectives and desired degree of separation across business units, product lines, functions, and geographies.

A successful divestiture management structure must define clear responsibilities and reporting relationships. Teams of specialists are tasked with managing the deal process, separating and rationalizing core functions, and optimizing the go-forward business model. A DMO has the overall responsibility for coordinating the divestiture. The DMO is responsible for coordinating actions across workstreams, ensuring cross-functional dependencies are resolved, monitoring resource needs, and reporting to an executive steering committee of senior leaders that provide oversight for the overall effort. Figure 2 illustrates what a divestiture and separation structure may look like.

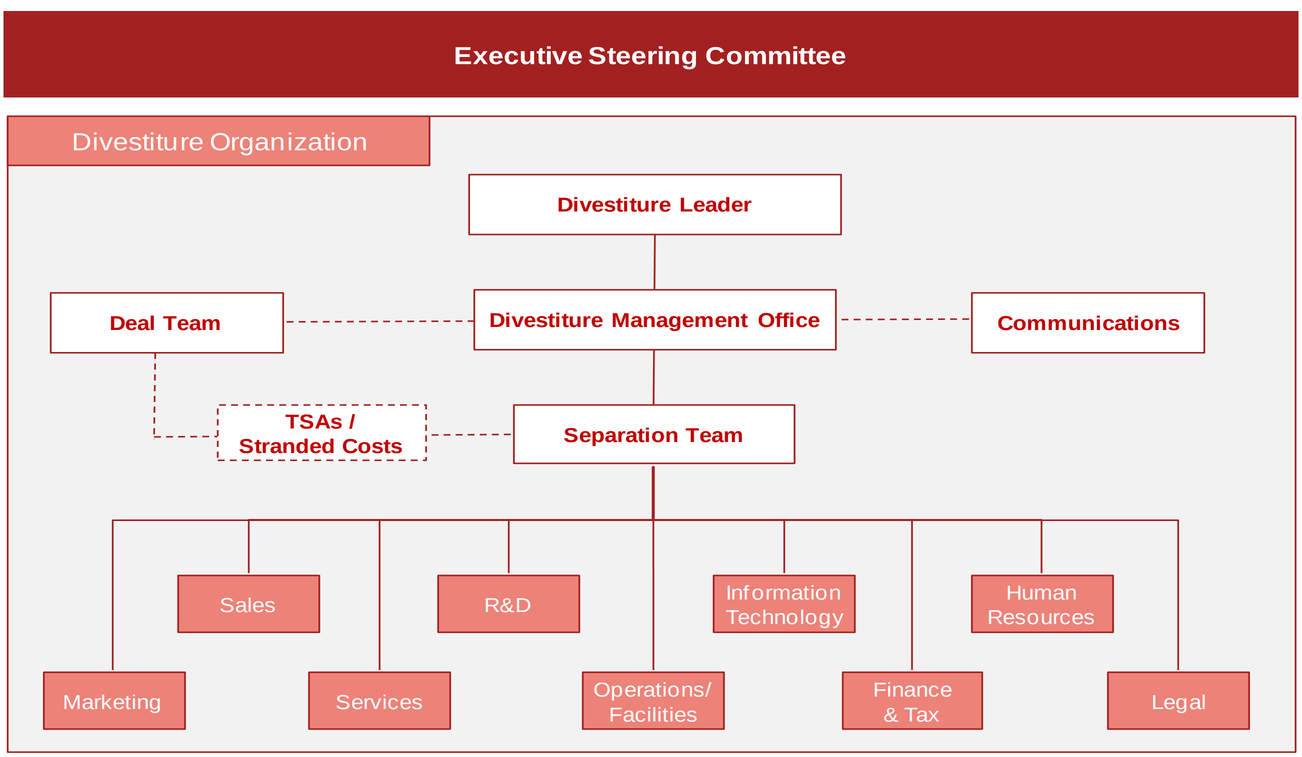

Figure 2 – The Deal Team is responsible for executing the external divestiture process. The Separation Team is responsible for executing the internal separation activities, "right-sizing" the remaining infrastructure, and supporting transition services. The DMO is responsible for optimizing overall results across the enterprise by balancing the three primary sources of deal value — transaction proceeds, transition costs, and Parent/Seller optimization. The DMO centrally coordinates activities across functions and geographies to ensure dependencies are identified and managed.

Resource needs for divestiture and separation activities are difficult to estimate. The number of resources required and the associated time commitment to accomplish the multitude of tasks often catch management by surprise. Also, since transition and separation requirements can be complex, particularly in large-scale divestitures, successful divestitures often demand prolonged commitments from an organization's best and-brightest, diminishing senior management's ability to manage the core business.

The DMO plays a central role in evaluating the level of resources required over the course of the transaction. Of critical importance is the need to balance divestiture and separation activities with ongoing business requirements to minimize disruption. One of the first matters to address is who will stay with the remaining organization and who will go with the divestiture. Other considerations include staff availability and bandwidth, the level and duration of their involvement, how to backfill the roles vacated by those serving in the divestiture organization, and the transition of team members back into their former (or new) roles once their involvement is complete.

Planning the Degree of Separation

Every organization is different, and every deal is different. It is critically important for the DMO to assist in defining what will stay with the remaining organization and what will go with the divestiture, establishing the degree of separation across functions and geographies, and effectively communicating this information to the divestiture organization. This will serve as the initial set of guiding principles each business unit or function will use to develop and execute detailed plans. Absent this guidance people will be unclear of their responsibilities and most likely miss required actions that may lead to transaction delay and ultimately, erosion of deal value. Also, a well-defined degree of separation establishes a clear starting point for negotiating the scope and duration of Transition Service Agreements with potential buyers, allowing the seller to better focus on pricing negotiations.

The degree of separation depends on various factors, including: transaction type, the type of buyer or buyers and their respective transition needs, how integrated the business unit or product lines to be divested are with the remaining organization, transitional requirements, and the potential for disruption to core business operations.

Separating infrastructure can be complex and present significant challenges, particularly when core operations are commingled — people, processes, systems, data, contracts, and facilities. Typically, stranded costs and post-closing transitional requirements are high when the business unit to be divested is significantly integrated across functions and geographies with the operations that will remain. On the flip side, if the business unit to be divested is operating as a standalone entity, the degree of separation will be low, with minimal or no stranded costs and post-closing transitional requirements.

Unlike during a merger or acquisition where the actual execution of the integration can, and often must, wait until the ink on the deal is dry, sellers don't have the luxury of waiting for close before starting the work of separation. Separation activities occur simultaneously with dealmaking. They are parallel efforts, not linear processes where one can begin only after the other is complete. Experience shows that sellers often wait too long before starting separation activities, increasing the likelihood for surprises late in the deal process which leads to closing delays and value erosion.

Communicating with Stakeholders

Key messages about the divestiture and separation need to be clearly defined and communicated, both internally and externally, addressing the special needs and concerns of each stakeholder involved. Communications should address the reasons behind the divestiture, describe the timing for key actions, and candidly explain both what is known and unknown. Communications should also articulate how the divestiture will benefit employees, customers, vendors, buyers, and investors.

While a communications team is often established to develop content and implement the communication plan, the DMO is responsible for launching and coordinating the communication process. Staging communications throughout the divestiture, and keeping everyone on the same page, is critical to ensuring a faster, smoother transaction and transition. A carefully orchestrated plan should be in place to proactively engage an expanding number of people throughout the deal process.

Plan divestiture and transition; Plan and execute Day One

Even if the best decisions are made as you "*Set the Course*," without proper planning and execution much can go wrong before transaction close. Value leakage can occur in many ways and experience shows that surprises and delays during the deal process often erode deal value. To mitigate value leakage, it is critical to ensure a fast-paced separation that makes early use of disciplined planning, a well-organized launch, and relentless focus on the priority initiatives that sustain and drive value.

Key areas for the DMO to address while planning the divestiture and transition include:

Launching the Divestiture

Ensuring an effective launch is the first step in mobilizing the divestiture organization. The DMO would typically invest a significant amount of time in planning a kickoff event — typically comprised of a series of meetings to ensure it is executed flawlessly. After all, this event often sets the tone for the entire divestiture. Getting the divestiture launch right is critical, since it is usually the first time people comprising the divestiture organization will collectively plan in a coordinated manner.

Typically, a divestiture kickoff event would include the following:

- Executive-level presentation on the divestiture rationale
- Explanation of scope for the divestiture, including business unit(s), product line(s), and geographic footprint
- Discussion of the potential types of buyers and how they may impact the deal
- Definition of the guiding principles based upon the desired degree of separation
- Primer on the divestiture organization structure and resources
- Overview of the role and processes of the DMO
- Break-out sessions that get functional teams working on defining divestiture activities, including scenario analysis for separation, transition services, and remaining cost structure based on the likely or potential buyers

The divestiture launch should be an "output driven" meeting where the functional teams focus on defining announcement, close, and post-close transition requirements and activities. Results of the meeting should also identify executive issues to be resolved and decisions to be made, cross-functional dependencies, and communication needs. Identifying potential "quick wins" for remaining infrastructure cost savings is another important outcome. The point is to leave the launch event with a defined set of objectives and activities by functional area, including tactical requirements for closing and the immediate transition period post-closing.

Developing the Workplans

The plans made and priorities set during the divestiture launch are key inputs to the workplan development process. Detailed workplans typically result in better divestitures and separations. But building comprehensive workplans take time, and companies often overlook the importance of this activity. Failure to invest the time and resources necessary to build these plans is typically another warning sign of divestiture failure.

Each functional team should develop workplans that spell out the tasks, resources, due dates, and cross-functional dependencies required to get the job done. These workplans are never static and should constantly evolve over the course of the transaction as new details become known and milestones achieved. In the early stages, the workplans should focus on the tasks most critical to transaction close and Day One transition requirements. This allows for timely identification of long-lead items well before they turn into closing-day surprises.

The DMO should work with each functional team to ensure sufficient workplan detail, and then review each workplan to promote consistency and completeness. In reviewing the workplans, the DMO should highlight dependencies, redundancies and critical path prerequisites, and assess resource gaps and requirements.

In addition to ensuring appropriate functional transaction and separation workplan development, the DMO should ensure proper coordination across the divestiture organization in the development of Transition Service Agreements and Stranded Cost Analysis.

- **Transition Service Agreements.** Experience shows that sellers often wait too long before identifying and documenting Transition Service Agreement (TSA) details. The result is a loss of negotiating leverage and deal value. Sellers should prepare for likely TSA terms and costs well in advance. Early TSA planning areas to consider include service level descriptions, duration, pricing and cost allocation methodology, dispute resolution and termination provisions, and performance tracking, invoicing, and payment processes.

- **Stranded Cost Analysis.** Stranded costs are those costs that will be left behind with the seller at transaction close and the expiration of transition services. Sellers should identify stranded costs early, while compiling stand-alone costs for the divestiture. This will allow for swift action on cost reduction initiatives. Understanding stranded costs and their impact on operations will also improve the Deal Team's negotiating position with potential buyers.

Rolling out Processes and Tools

During the early phases of a divestiture, an effective DMO will introduce the broader divestiture organization to common processes, tools, and templates to ensure the divestiture and separation activities are executed in a coordinated manner. The job of the DMO is not to perform the detailed work of the divestiture, but to coordinate its completion by the business unit and functional teams.

An effective DMO manages by exception. If the divestiture launch is a success and workplans are finely detailed, then the DMO can move to an "exception-based management" approach. A DMO can accomplish this approach through the use of several key processes, including regular status reporting and dependency management and tracking.

- **Status Reporting**. A periodic reporting cadence is established with the functional teams using standard reporting templates designed to capture progress on key milestones, decisions to be made, issues to be resolved, and cross-functional dependencies to be managed. A typical reporting cadence is weekly through transaction close, and either monthly or bi-monthly thereafter, depending on the level of transition services being delivered post-close and the extent of reorganization required in the remaining company operations.

- **Dependency Management**. A dependency is a need by one functional area for action, information, or decision-making from another functional area. Generally, a dependency must be satisfied by one function before the other function can move forward with an aspect of the transition or separation effort. Managing dependencies across functions can be complex, confusing, and time consuming. But the activity is similar to tightening the lug nuts after rotating the tires on your car — if you don't do it, the wheels will come off. In a smaller transaction, the use of a simple dependency log may be all that is required. However, in larger scale and cross-border transactions, a more rigorous process and set of tracking mechanisms may be needed. In either case, the primary goal is to ensure dependencies are identified and properly assigned to those tasked with resolving them in time to prevent deal delay.

Role of the Deal Team

Companies frequently struggle to manage the blistering pace of deal negotiations while simultaneously addressing the significant operational and separation requirements that accompany a divestiture. This raises the question of who should lead the Deal Team and the Divestiture Management Office (DMO), and how the two groups interact. Though no two companies are the same — with varying levels of deal sophistication, divestiture experience, and operational expertise — understanding and coordinating the respective roles and timing of the Deal Team and the DMO are critical to managing a successful deal process.

The Deal Team is the first group involved. It is comprised of individuals from Corporate Development who have most likely identified the business unit or product line to be divested and examined the marketability of the assets. The Deal Team's activities normally begin before the DMO is formally launched and are largely complete by transaction close. However, both the Deal Team and DMO are in existence leading up to transaction close, when resource demands are highest.

As every deal is unique, no hard and fast rules exist for Deal Team and DMO coordination. But certain leading practices increase the probability of divestiture success:

- The Deal Team should engage the anticipated DMO lead in early planning activities. This provides the DMO lead with institutional deal knowledge and enables the seller to efficiently define guiding principles and operating assumptions.
- The Deal Team and DMO should have separate reporting lines and scheduled updates to executive management (often the Steering Committee). This is necessary due to the complexity and volume of information that needs to be communicated.
- On complex transactions, financial information to be provided to potential buyers is critical for deal negotiations. Accordingly, the Deal Team should oversee the financial statement carve-out process and data room requirements scoping with operational support from the DMO.
- Once the deal process is under way, the DMO should work with the Deal Team to manage the follow-up diligence request list and stage buyer requests (especially during an auction process). The DMO has the best visibility to critical resources working on operational and IT separation; therefore, the DMO is in the best position to prioritize requests and reallocate resources to balance competing operational demands during deal negotiations.
- Leadership should establish a clear communication protocol and feed-back loop between the DMO and the Deal Team to filter information provided to the functional and business unit teams executing the transition, preventing information overload to the teams. Message consistency and a clear end goal are critical for operational teams to be successful. Likewise, issues impacting transaction timeline, deal value, and TSA service levels identified by the DMO need to be effectively communicated to the Deal Team.

Design and implement the future state; Execute transition

Delivering an effective divestiture — and optimizing overall results across the enterprise — involves balancing three primary sources of value: transaction proceeds, transition costs, and Parent/Seller optimization. While the Deal Team is responsible for executing the external divestiture process and realizing the highest transaction proceeds, this activity is largely complete upon transaction close.

When it comes to delivering transition services, eliminating stranded costs, and realizing sustainable long-term operating model effectiveness, transaction closing is just the beginning. In larger divestitures with significant separation requirements, the DMO is responsible for implementing centralized processes for these complex areas, and must continue to drive coordination across functions and geographies to achieve post-closing objectives.

Key areas of focus for the DMO during this phase include:

Delivering on Transition Service Agreements

Since the time needed to complete separation requirements often exceeds the divestiture timeline, buyers typically require some sort of transitional services from the seller for a period of time after the transaction closes, and the seller charges for the services at a negotiated price. Common areas include information technology support, transaction processing support, and facilities, among others.

As part of the separation planning process, sellers should plan for likely Transition Service Agreement (TSA) terms and costs well in advance. Sellers that wait too long before identifying and documenting likely TSA details often get caught on the wrong end of the bargaining table, and fall behind on the targeted transaction timeline. As each day passes, TSA details are more commonly developed and negotiated in a way to simply get the deal done, leading to difficulties for both parties and often resulting in value erosion for the seller.

In addition to lack of early planning and preparation by the seller, complexities may also arise for other reasons, including:

- Not knowing the identity of the ultimate buyer and their exact transition requirements at the time separation planning commences
- The physical difficulty of unwinding assets that have been carefully integrated over the years, particularly information technology applications
- The logistical difficulty of gathering necessary service level and costing information from multiple functions and geographies

The DMO is instrumental in overcoming these complexities and helping to formulate and launch TSA planning efforts, serving as the central coordinating point for all functions and geographies in developing and negotiating the TSA. The DMO is responsible for working with each functional and geographic leader to identify TSA requirements as part of the separation planning and workplan development process. The DMO can also continue to play a critical role post-close in monitoring the progress of service delivery to mitigate value loss due to service level decline or untimely handover requirements.

Reducing Costs

Too often, companies fail to effectively address cost-reduction opportunities as part of the divestiture and separation process. After all, executing a divestiture is hard enough when resources are already constrained. However, failure to eliminate stranded costs and optimize the remaining company cost structure post-close can have essentially the same negative effect on shareholder value as reduced transaction proceeds. Additionally, an opportunity may also exist to demonstrate a lower cost structure for the divested business, which can lead to an increase in transaction proceeds.

Planning for these cost reduction opportunities requires a concerted effort; experience shows a formal cost reduction program should be part of the divestiture plan from the beginning. Again, the DMO is in an excellent position to formulate and launch these cost-reduction efforts as part of the separation planning and workplan development process.

Designing and Implementing a New Operating Model

A divestiture can present a wealth of new opportunities by forcing an organization to review its strategy, processes, and scale, particularly in larger divestitures where a significant portion of overall revenue is carved-out out. In fact, the divestiture process itself is often a by-product of a portfolio review performed by management to identify businesses not generating sufficient returns or no longer fitting into the company's strategic plan for the future.

However, planning for and executing a new business model is generally disconnected from the divestiture and separation process, running as a parallel effort. This can create unintended consequences, including bringing back costs that the DMO and Parent/Seller have worked hard to reduce or eliminate.

Experience shows that combining divestiture separation, transition, cost reduction, and go-forward operating model efforts in a centralized program effectively synchronizes these enterprise-wide activities for quicker, more impactful overall results. Once again, the DMO is in an excellent position to formulate and launch these efforts, effectively prioritizing initiatives that will lead to the highest financial impact in the shortest period of time with the highest probability of success.

Conclusion

A disciplined approach to divestiture is critical to deal success. A well-defined divestiture process and set of fundamental activities rolled out by the DMO helps achieve early wins, build momentum, and instill confidence among stakeholders. Adherence to a well-planned divestiture process and recommended set of DMO activities, as outlined in this paper, can guide companies along the path to a successful divestiture and allow managers to focus their efforts on sound execution.

Acknowledgements

For a deeper discussion on the content of this paper or other deal considerations, please contact one of our practice leaders or your local PwC partner.

Authors:

Barrett Shipman, Principal
US Divestitures Operational Readiness Leader

Gregg Nahass, Partner
Divestitures Operational Readiness

Paul Hollinger, Principal
Divestitures Operational Readiness

Deals Team:

Martyn Curragh, Principal
US Deals Practice Leader
646 471 2622
martyn.curragh@us.pwc.com

Colin Wittmer, Partner
US Divestiture Services Leader
646 471 3542
colin.e.wittmer@us.pwc.com

Barrett Shipman, Principal
US Divestitures Operational Readiness Leader
512 708 5651
barrett.j.shipman@us.pwc.com

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