Viewpoints

Managing the People Challenges in Divestitures

By Kelly Karger

Although divestitures of any form (such as a sale of operations or spinoff) can play a crucial role in shaping a company's business portfolio and ensuring long-term profitability, they will fall short of expectations if the seller fails to retain and motivate key employees through closing.

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Recent Willis Towers Watson research finds that most companies have lost shareholder value from divestitures.* The reasons vary, but weak performers tend to underestimate the cost and complexity of divestitures, including its impact on employees who are needed to ensure the success of the business.

If divestments have significant potential value as part of a broader business strategy, what can companies do with their human capital to improve the odds of a successful outcome?

People-related challenges can have just as much impact on the success of the divestiture as they do on the success of an acquisition.

Why divest?

Determining whether to divest a business involves a complex process that considers how the action will fit into larger enterprise objectives. As strategic divestments are identified, the focus turns to the best approach to removing the business, whether through creating a stand-alone entity (let's call it "SpinCo"), or selling the business if suitable buyers are available.

Part of the business case is devising a separation process that is flexible enough to change as the divestiture progresses. Although planning may initially assume a spinoff, an outright sale might become a more attractive option if potential buyers become interested and available. By the same token, a company can pivot from a potential sale to a spinoff if no acceptable buyers surface, although this is much less common. It is relatively easy to begin preparing for a spinoff and pivot to a sale if a buyer emerges. However, it is much harder to prepare for a sale and pivot to a spinoff. Often this will mean a significant change to the timeline because much of the preparatory work for a spinoff hasn't been done while preparing for a sale.

While divestitures follow the same deal life cycle as acquisitions, as the seller there's a different focus and activities in each phase. However, one constant is the fact that people-related challenges can have just as much impact on the success of the divestiture as they do on the success of an acquisition.

In this article, we outline the challenges and pitfalls to look out for when it comes to often overlooked people issues at each phase of a divestiture, whether it's a spinoff or an outright sale.

*Willis Towers Watson Divestment Performance Monitor, April 2019

Divestitures are not acquisitions in reverse

You've probably heard the phrase "Divestitures are not acquisitions in reverse." One of the key reasons for this is that divestitures are typically more emotionally challenging and lack the celebratory nature of an acquisition. Change management plans must reflect this reality and include robust stakeholder identification across both the divested business as well as the remaining business. Here are some tips around key challenges.

Key challenge: retaining leaders and key talent

A common misconception is that retaining leaders is mostly about money. In actuality, our research* shows that the most commonly cited reasons for leaders and key talent leaving after a transaction are discomfort with the culture of the new organization, aggressive pursuit by competitors, and dissatisfaction with their new role or with the strategic direction of the new company. Involving key talent in shaping the culture of the new company, setting clear expectations and ensuring they understand how their roles contribute to the organization's success will help – if leaders and other key talent are engaged, they will be less likely to entertain offers from competitors.

*Willis Towers Watson 2017 Global M&A Retention Study

Key challenge: talent selection

Defining and communicating an effective selection process should be a pre-close priority. Creating organization charts that clarify the structure of the new business, specify the number of employees, roles and locations, will be key. The next step is to define the selection process to fill those roles. Getting position descriptions and reward packages ready in advance helps make the talent selection process more agile.

Key challenge: change management

Preparation timelines are often lengthy and uncertain. To combat the inevitable stress this causes employees, it helps, once the key parameters of a plan are in place (including the bulk of the Total Rewards approach and selection process) to communicate that plan to key stakeholders. These include both the employees who will be staying with the parent company and those who will be moving to the new one.

Key challenge: communication

Equip leaders and line managers across the business with talking points to help them consistently, clearly and easily articulate the business rationale for the divestment, and what's changing for employees. In particular, focus on the "what's in it for me" information: reporting relationships, pay and benefit-related changes.

Phase: Due diligence (pre-announcement)

Prior to public disclosure of divestiture plans, substantial groundwork is needed to position the business to draw the best possible offer and related terms. In addition to preparing to respond to any buyer data requests, pre-announcement planning involves clearly defining the in-scope employees and fully understanding "entanglements" between the parent company and the business to be divested. People-related entanglements are common in compensation and benefit programs, HRIS and payroll, administrative systems, and talent sourcing and recruiting.

A divestiture is most likely to fall short of expectations when pre-announcement planning is conducted only as a "check-the-box" exercise, or only focused on the financial components. On the contrary, the planning must be driven by the specific deal hypothesis and business strategy behind the deal, and must account for the divestiture's effect on the remaining business. Other success factors include the ability to understand buyer profiles – and to respond quickly as new potential buyers emerge during the divestiture process.

Whether the divestiture will be a spinoff or sale, if there are people involved there will be an Employee Matters Agreement. At the due diligence phase, sellers should:

- Establish clear deal and people separation principles in order to define a strong negotiating position with regards to all people-related matters. The entanglements will play a role in what you are willing and able to negotiate, including where Transition Services may be needed. In some cases, steps can be taken to start disentangling as part of this preparation.
- Develop an effective change management strategy and retention plan for key clients and employees who may be affected by the divestiture. By the time of a public announcement, management must be in a position to move quickly to address employee and client concerns that might diminish the value of the business before close.

Phase: Separation planning (between announce and close)

Once the transaction is announced, attention shifts to an effective and efficient transition, with rigorous management of a budget and resources. Transition execution requires not only implementing plans to separate the divested business but also understanding what the buyer or SpinCo should be doing, and addressing the impact of the separation on the remaining business. Each party must be held accountable for its defined role and the resources devoted to the transition.

Without this rigor, sellers' pre-announcement planning can be undermined by inexperienced buyers, delaying the close or expanding the need for Transition Services. Failing to devote appropriate financial and leadership resources leads to delays and errors, inadequate communication to employees, and diminished value of the business.

People-related separation activities must be treated with care due to the potential direct impact to employees and their families. At this stage:

- Depending on the required treatment under the Employee Matters Agreement, separation plans should factor in sufficient time to implement. When sufficient time is not possible pre-close, Transition Service Agreements (TSAs) are often used to allow for separation post-close. Now is the time to set up the processes for both implementation and the exit plans for the Transition Service Agreements.
- Through all of the separation work going on, employees should have the same experience and leadership of the business until the divestiture is finalized at close. Because divestitures are emotionally challenging transactions, the employee experience must be treated with intent.

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Phase: Separation execution (post-close)

After closing, TSAs will go live and it's common to breathe a sigh of relief as the seller. But not so fast, the goals of the divestiture haven't been realized yet. In addition to rigorous administration of the TSA and implementing TSA exit processes, attention must include optimizing the remaining organization:

- This is the time to take concrete steps to align with the reduced business size and future business goals as identified at the due diligence phase. Take the time to review how each function is supporting the remaining business, and move quickly to deal with any stranded costs or processes that should be adjusted to realize the business goals of the divestiture.
- Don't forget that the remaining employees may still be in a period of uncertainty, wondering if their business is next and how the optimization activities will impact them. Those working on the TSA administration will be concerned about the future of their roles. Change management at this stage should reinvigorate and reinforce the future business strategy and address employee distraction and loss of productivity.

With thorough planning and preparation pre-announcement, sellers can use the time more wisely to execute and transition to the buyer (or stand-alone company) faster and more cost-effectively. Post-close, all attention can turn to optimizing and unlocking the real value of the divestiture.

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