

A Definitive Guide
Building Great Boards for Corporate Spinouts and IPO's

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The Following are excerpts from the above titled brochure, available upon request to qualified prospective clients.

An Executive Search Perspective

The challenges of recruiting a board for the new company are often underestimated in the initial planning stages of a spinout. As the focus centers on legal and accounting issues, board recruitment may be accorded insufficient time.

Success in recruiting directors for spinouts and IPOs requires a compelling board opportunity and a disciplined process. The planning process for assembling a board should begin as soon as possible. Creating a new board will take 3 to 6 months.

Corporate governance practices have positioned director selection squarely in the spotlight. Expertise, independence, and diversity will be closely examined.

The ability of a new company to assemble an impressive board is a key indicator to investors of the company's potential success.

There are 10 critical steps to building great boards for corporate spinout and IPOs. Each is described in depth in our brochure "Building Great Boards for Corporate Spinouts and IPOs."

A spinout board, when structured appropriately and built professionally, is immensely beneficial to the company and reflected in shareholder value.

The creation of new public companies through Corporate Spinouts and Initial Public Offerings (IPOs) continues at a very active pace in the United States and elsewhere around the world. On an international basis, according to reputable sources¹, the number of completed domestic corporate spinouts annually, between 1995 and 2006, increased from 55 to 73; and the number of global IPOs increased from 1,290 to 1,729 during that same period.

Heightened Scrutiny
Regarding Director Selection

Corporate governance practices have come a long way. Board composition and board director selection are centered in the spotlight. Activist shareholders and institutional investors now fully expect, and demand, that boards will be populated with independent directors and that board composition will be diverse. While director acumen is less often mentioned as a concern, the

¹ Ernst & Young, Global IPO Trends Report 2007; Thomson Financial SDC Platinum

professional accomplishments, seasoning, and reputation of directors should always be the first consideration. The ability of a spinout or IPO to assemble a board that is an impressive blend of acumen, independence, and diversity is often a key indicator to potential investors of a company's success potential and orientation toward the best interests of the shareholders.

Planning for an Issue-Free Spinout on Day-One

Deborah L. DeHaas, Vice Chairman and Midwest Regional Managing Partner
Thomas D. Williamson, M&A Principal
Deloitte LLP
Chicago, IL

What are ways to reduce natural tensions between the parent and the spin?

- It is important that the parent and spinout agree on some “guiding principles” to be kept in mind when making tough mutual decisions. One of our clients was guided by the principle that “all such decisions would be ‘economically neutral’ to both parties.”

What are the solutions for the challenges in doing a spin?

- Careful forethought and skilled planning is what we advise for our clients. The practices of establishing an effective governance structure and specifically having the “right” board in place to oversee the management and the strategy of the new spinout organization. In addition, developing a divestiture roadmap and end-state blueprints, minimizing dependency on TSAs, and focusing on Day-One readiness are all critical to success.
- It is also essential to strive to achieve an efficient cost structure that allows the spinout company to focus on the core business, as well as to manage any negative impact on customers and employees.

Thoughts from a Spinout Chairman

Dennis D. Dammerman
Chairman, Discover Financial Services (NYSE)
A Spinout of Morgan Stanley, June, 2007

Professional Assistance:

Get professional help in assembling a new board. Sit down with a search firm to define the desired makeup in terms of skill, experience, fit, and collegiality; and then start the process of finding individuals who fit the criteria.

CEO Directors:

It is important to have public company CEOs, retired or active, on the board. We have 5 CEOs on our board – 3 retired, 1 active, and 1 an entrepreneur. They bring public company experience at the highest management level, and bring a deep understanding in governance, compensation, and communication with share-holders.

**Factors to be Considered in the Director
Candidate Screening Process**

- **Professional reputation** and years of board service remaining until retirement.
- **Willingness to commit** the time required for responsible service.
- **Courage to communicate** one's views honestly and respectfully.
- **Maturity to listen** well, acknowledging the views of others, even when they differ from one's own viewpoint.

CULTURE FIT

It is important that candidates be considered a "good fit" to the culture or chemistry of the board. This is not to suggest that the selection committee is looking for directors who will be easy or rubber-stamps, but rather that they are mature, seasoned professionals who will be effective.

A Guidepost for the General Counsel

Kelly McNamara Corley
EVP, General Counsel and Secretary
Discover Financial Services, Inc. (NYSE)

What did you learn?

Organization is key. Our transaction moved very quickly. Time management and a cohesive team are critically important.

Is assembling the board a complex task?

It is like putting a puzzle together. You have to be continuously focused on the richness and desired balance of the board as it is being assembled. If you are trying to meet ten different selection criteria, and the first four directors you pick have similar profiles, you have backed yourself into a corner. JamesDruryPartners' "pinwheel" model helped us stay on course.

When should you start the recruitment of board directors?

You should start immediately, for a variety of reasons. You need time to thoughtfully develop the director selection criteria. It will take a fair amount of time to develop a list of director candidates who meet the criteria. If looking for ten, you may need a list of 100 or more possibilities. The interview process will also take quite a while.

A Lawyer's Perspective

Christine A. Edwards, Capital Partner
Winston & Strawn LLP
Chicago, IL

What do clients most risk getting wrong at the beginning of the spinout planning process?

It is common for the management team to underestimate the amount of time and substantive work involved when taking a company public. The time it takes to recruit directors is at the top of the list, in my opinion. Management also tends to minimize the time required to address certain "social issues".

What are management's requirements for directors?

Management should select as many new directors as possible prior to the spinout.

- If only four independent directors are identified, it may be difficult for these directors to handle the work of the three major committees.
- As board directors assume the full weight of board fiduciary responsibility for the new company upon being elected, they will want to share this responsibility with a larger group of directors.
- Practically speaking, it will also be easier to recruit other directors if a larger group has been identified.

Spinout Reflections

William R. Johnson, Chairman and CEO,
H.J. Heinz Company
Business unit spinout into merger
with Del Monte (NYSE)

In doing a spinout, you're trying to create a successful new company without the historic support of the “old” parent company.

Biggest Challenge: Assembling a team of directors that can work well with the new management team.

Needed Director Attributes: Having more patience than normal, being attuned to the strategic planning needs of a new company, and being able to work with a management team that may be new to the public markets.

When to Start Recruiting Directors: Immediately - right after launching the spinout planning process. It always takes longer to recruit directors to a new public company than to an established one.

SUMMARY

Obstacles and bumps in the road will surface for every new company, but can be more easily addressed and overcome with the help of a strong board. There is no substitute for expending the time to assemble a spinout or IPO board in a highly disciplined and professional manner – to do anything less could dilute the promise of even the best new company.

When done well, the newly assembled spinout or IPO board will earn more than a fair return on its investment. The strength and reputation of the board can translate into a highly receptive initial market for the spinout company's stock. The new company may benefit from a higher level of trust and loyalty felt by customers, suppliers, and employees.