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**Private Information and Bank-Loan Pricing:
The Effect of Upcoming Corporate Spinoffs**

Ole-Kristian Hope †

Rotman School of Management, University of Toronto
okhope@rotman.utoronto.ca

Vlad-Andrei Porumb

Accounting and Finance division
Alliance Manchester Business School, University of Manchester
vlad-andrei.porumb@manchester.ac.uk

Simona Rusanescu

Department of Accounting and Auditing
University of Groningen
s.rusanescu@rug.nl

Dushyantkumar Vyas

Department of Management - UTM
Rotman School of Management, University of Toronto
Dushyant.Vyas@rotman.utoronto.ca

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†Corresponding author.

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Abstract

Corporate spinoffs are important events that are accompanied by valuation and credit-risk implications for the parent firm. Among other benefits, spinoffs can improve corporate focus and enhance valuation transparency. In the debt-contracting context, however, spinoffs can also be associated with negative outcomes for the divesting firms. We examine whether banks, due to their timely access to material private information, are able to ascertain the likelihood and the implications of impending spinoffs for the parent firm *before* a formal public announcement of the spinoff. Our empirical analyses indicate that, in the 365-day pre-spinoff announcement period, banks charge incrementally higher (lower) spreads to borrowers with increased (decreased) post-spinoff riskiness relative to non-divesting firms. This suggests that, while lenders recognize the value- and transparency-enhancing effects of spinoffs, they are also able to foresee potentially negative implications of these divestitures. Cross-sectional analyses indicate that banks charge incrementally lower loan spreads if spinoffs result in high-risk borrowers having either higher reporting quality or lower reporting or operational complexity. These results suggest that the post-spinoff increase in riskiness is compensated by the divestiture benefits typically associated with spinoffs. Similarly, high-risk borrowers incur larger spreads if they do not undergo “focus-increasing” spinoffs. Overall, our findings suggest that banks are able to *ex-ante* determine the implications of important corporate events such as spinoffs.

Keywords: Spinoffs; Bank-Loan Pricing; Private Information; Financial Reporting Quality; Complexity; Ex-Ante Analyses.

Private Information and Bank-Loan Pricing: the Effect of Upcoming Corporate Spinoffs

1. Introduction

Conglomerates are valued at a discount relative to less diversified firms (Berger and Ofek 1995; Servaes 1996; Shin and Stulz 1998), either because over-diversified firms invest inefficiently (Rajan et al. 2000) or because they are hard to value due to increased complexity and information asymmetry (Krishnaswami and Subramaniam 1999). In response to this potential conglomerate discount, some firms adopt a specialization strategy by engaging in divestitures, which allows them to refocus on their core business. Divestitures, such as corporate spinoffs, asset sales, and equity carve-outs can reduce business complexity, and thus, facilitate the discovery of the true market value of firms' segments (Chemmanur and Liu 2011). Further, different business segments may appeal to different groups of investors, and divestitures can assist market activity by matching business and investors more appropriately and efficiently (Vijh 1994). This enables separate divisions to attract additional capital, as investors are better able to conduct fundamental valuation.

The use of spinoffs to divest businesses has become increasingly frequent. A spinoff offers several potential benefits, such as avoiding over-diversification problems, providing higher operational focus for the newly separated entities, and reducing information asymmetry (or higher valuation transparency) regarding the component business units (Rajan et al. 2000; Krishnaswami and Subramaniam 1999). By conducting a spinoff, the firm intends to let the capital markets discover value in one or more of its divisions by allowing them to trade separately. For example, spinoffs enable high-growth divisions, once separated from other low-growth divisions, to receive higher valuations.

The implications for *creditors* are less straightforward. Studies find that bondholders either gain (Veld and Veld-Merkoulova 2008) or lose (Maxwell and Rao 2003) after corporate spinoffs. The positive effect is attributed to increases in post-spinoff market valuation, whereas the negative effect is due to potential wealth transfers from bondholders to shareholders. While spinoffs are

relevant events for all lenders, due to potential reductions in their borrowers' risk diversification and overall asset base, the literature has so far been silent regarding private debtholders' (i.e., banks) views about spinoffs. We examine whether banks' superior information access enables them to recognize the potential benefits and negative implications of upcoming spinoffs *before* the actual event.

Banks' superior monitoring ability has long been recognized, such as in the seminal work by Diamond (1984) on delegated monitoring. For example, lending relationships and contracting provisions enhance the monitoring capacity of banks over borrowers' operating and financial activities (e.g., Diamond 1984; Ramakrishnan and Thakor 1984; Fama 1985; Shleifer and Vishny 1997). Further, banks are documented to have *superior access* to information from non-public sources (Sharpe 1990; Denis and Mihov 2003). Because of this feature of lending arrangements, banks are able to partially compensate for any limitations in their borrowers' financial reporting quality during the due diligence process (e.g., Biddle and Hilary 2006). Thus, assessing the creditworthiness of borrowers represents banks' primary advantage over other types of creditors, as they are likely to have *superior ability* to collect and assess disclosed public information as well as access to private information relative to other less sophisticated market participants (Bharath et al. 2008).

Spinoff announcements are, in general, publicly unexpected (Augustin et al. 2020). Therefore, banks' potential access to inside information is likely to enable a timely and accurate assessment of the value and risk implications of an upcoming spinoff.¹ Specifically, to avoid potential wealth transfers from creditors to shareholders (Parrino 1997; Maxwell and Rao 2003), banks may estimate the value implications of a forthcoming spinoff – from an operational and transparency perspective – and adjust lending terms accordingly. Nonetheless, whether lenders will use information about impending spinoffs in loan pricing is not clear *a priori*. For example, having

¹ We provide evidence of banks including information regarding forthcoming spinoffs in loan contracts. Please see section 1 of the Supplementary Appendix for loan contracts excerpts.

access to private information may not be sufficient to allow banks to estimate the value and risk implications of upcoming spinoffs. On the one hand, private information could be biased by the incentives of borrowing firms to provide favorable information regarding their future prospects. On the other hand, we acknowledge the possibility that lending terms will not impound private information if it is simply not provided by the borrowers in a timely manner. Additionally, it is possible that banks learn about upcoming spinoffs from other capital market participants – such as equity investors and bondholders – if these participants are able to obtain such information from unspecified sources. This expectation is, however, inconsistent with research documenting on-average insignificant reactions from other market participants prior to the spinoff announcements (Veld and Veld-Merkoulova 2008). Overall, controlling for other concurrent factors, if banks adjust the spreads of loans extended *before* a spinoff public announcement, the divestiture information is likely obtained via their private information channels. We further posit that banks are able to estimate and price the probability and risk implications of the spinoff *before* its public announcement. Moreover, we expect that banks are likely to adjust loan pricing depending on borrowers' *ex-post* change in riskiness.

To test our expectations, we use a sample of 50,619 loan facilities of U.S. firms originated between 1986 and 2017, out of which 259 loans are granted to firms with upcoming spinoffs. We find that, in the one-year pre-spinoff period, on average, loan spreads are insignificantly associated with upcoming spinoffs. Nonetheless, when we distinguish between upcoming spinoffs conditional on their effect on divesting firms' credit risk, of which 20 (239) loans are extended to firms whose credit risk deteriorates (does not deteriorate), the results suggest that banks penalize (reward) firms that (do not) increase their riskiness after the spinoff, by charging incrementally higher (lower) spreads. This result indicates that banks use their private communication channels to infer information regarding the forthcoming divestiture and adjust the interest rate according to the expected outcome of the spinoff. In terms of economic significance, the pre-spinoff spread charged on loans to high-risk (non-high-risk) spinoff firms increases (decreases), on average, by 126 (13)

basis points relative to non-divesting firms. In addition to including numerous controls and lead-bank fixed effects in our main analyses, in robustness tests, we also consider firm fixed effects, entropy balancing, robust regression, instrumental variable (IV) analysis, as well as a test where we restrict the sample to only include loans of firms with spinoffs during the sample period. We find consistent results across these alternative model specifications.

We conduct several cross-sectional analyses, showing that the effects of an upcoming spinoff are contextual. Specifically, we use constructs that gauge (1) the *ex-post* changes in borrowers' reporting quality and reporting and operational complexity, and (2) the spinoff type. We focus on these contingencies because they capture important divestiture outcomes which are likely to have a differential incremental impact on the pricing of forthcoming high-risk and non-high-risk spinoffs. First, we assess how spinoff firms' reporting quality and organizational and informational complexity impact loan pricing. More complex or low reporting quality firms are generally associated with both higher information and monitoring costs and greater operational inefficiencies (Bushman et al. 2004). Given the focus of lenders on downside risk, companies that improve their reporting, information, or operational efficiency post-spinoff will likely compensate for the negative effects of the increased credit risk and consequently are likely to be penalized less by banks. In line with our expectations, the results suggest that high-risk spinoff firms that either improve their reporting quality, reduce reporting complexity, or reduce operating complexity, have incrementally smaller spreads. In contrast, the *ex-post* changes in the quality of financial reporting and complexity of reporting and operations have no differential impact for non-high-risk firms undergoing a spinoff.

Second, we assess if the spinoff type affects loan pricing. Specifically, we split spinoff firms depending on whether borrowers undertake a focusing or a non-focusing spinoff. The benefits associated with focusing spinoffs are incrementally larger, as this type of spinoff enhances both the parents' and spun-off entities' post-spinoff operational performance and transparency (Hite and Owers 1983; Campbell et al. 2020). Our results suggest that high-risk borrowers that do not undergo

focusing spinoffs have incrementally higher spreads in the pre-spinoff announcement period. Overall, the results of our cross-sectional analyses indicate that reporting quality, reporting and operating complexity, and spinoff type have incremental (insignificant) effects on the pre-spinoff loan pricing of high-risk (non-high-risk) borrowers. We attribute this asymmetrical effect to banks' focus on borrowers' downside risk that is, at least partly, compensated for by the information and operational benefits of spinoffs.

Finally, despite the documented benefits of corporate spinoffs, it is likely that lenders are wary about the potentially adverse effects of spinoffs on borrower credit quality. Banks may therefore protect themselves from adverse credit quality effects of spinoffs by using additional financial and non-financial covenants in loan contracts. However, banks may provide contractual flexibility in loan covenants to allow the spinoff to take place while charging a significantly higher spread to compensate for the increased *ex-post* risk. Our additional analysis suggests that the loans granted to both high-risk and non-high-risk firms have fewer covenants in the pre-spinoff announcement period. This result is consistent with banks' focus on contractual flexibility in loan covenants for borrowers with impending spinoffs.

Our study contributes to the literature on debt contracting by providing evidence that banks can estimate the probability and outcome of important future corporate events such as spinoffs and adjust their pricing accordingly. Specifically, this paper provides empirical evidence that banks, due to their information advantages, adjust loan pricing *before* the public announcement of forthcoming spinoffs. We therefore identify information conveyed through alternative channels, such as loan pricing, that is not readily reflected in traditional financial reports and disclosures issued by firms. A related study by Plumlee et al. (2015) documents that banks price private information on impending patents before their public disclosure. Unlike spinoffs, patent applications represent inherently positive news for the borrowing firm (Plumlee et al. 2015). In contrast, our focus is on spinoffs – major corporate events that involve costly restructuring of the firm (Hite and Owers 1983; Campbell et al. 2020) – which, despite their associated benefits, could

also have negative consequences for creditors (Parrino 1997; Maxwell and Rao 2003). In our view, these unique characteristics highlight the importance of spinoffs as a highly consequential restructuring activity with differential credit-risk implications, and thus differentiate our study from prior work related to bank monitoring.

Second, we add to the spinoff literature by showing that banks, as sophisticated investors, can assess and value the potential risks and benefits of spinoffs. More importantly, our results suggest that the adjustments in loan spreads are observable for borrowers with both adverse or positive post-spinoff credit outcomes. Research has so far only assessed the impact of spinoffs for public debtholders (bondholders), without reaching a consensus (Parrino 1997; Maxwell and Rao 2003; Hite and Owers 1983; Dittmar 2004; Veld and Veld-Merkoulova 2008). Research has not yet examined how private debtholders – benefiting from both (1) superior ability to analyze publicly available information and (2) access to borrower information, from inside or non-public sources – assess this type of divestiture. This is perhaps surprising given the prevalence and importance of spinoff transactions in the U.S. capital markets in recent years (Campbell et al. 2020).

Notably, our study also suggests that, in the 365-day pre-spinoff announcement period, there are incremental benefits that accrue to high-risk borrowers with (1) increases in financial reporting quality, (2) decreases in reporting or operational complexity, and (3) focus-increasing spinoffs. These findings add to both the spinoff and debt contracting literatures, providing strategic implications for companies going through divestitures. Our results extend research on informed trading surrounding spinoff announcements (Augustin et al. 2020; Charoenwong et al. 2016) to the primary syndicated loan market, and show that “temporary insiders,” such as banks, incorporate the potential effects of forthcoming spinoffs in their pricing decisions. By documenting loan-spread adjustments in the one-year pre-spinoff period, our study provides empirical evidence suggesting that the information regarding the impending divestitures is available to firm insiders before the public spinoff announcement date. Finally, we provide additional empirical evidence on the important effects of financial reporting quality by demonstrating its continued value-relevance

implications even in the context of transactions where non-public information presumably plays a major role for contracting parties.

2. Institutional Background and Hypotheses Development

Spinoffs tend to involve significant financing transactions, such as new loan agreements or the amendment or refinancing of existing debt to avoid default or to adjust the loan-contracting terms to the new capital structure of the resulting firms (please see Appendix 1 for additional institutional background on corporate spinoffs). Given the critical role of creditors in the success of a spinoff transaction, discussions with potential financing sources normally start early in the planning process of a spinoff (Wachtell et al. 2016). We contend that this negotiation process is a potential mechanism for banks to access valuable private information concerning forthcoming spinoffs.

The public announcement of the intention to carry out a spinoff (at time t) is typically made well in advance of the date when the spinoff becomes effective. According to Gibson Dunn (2018), it takes about six months to complete the divesting transaction (i.e., spinoff effective date is $t+6$ months). Although preliminary discussions start early in the spinoff preparation process, the timing of the public announcement (t) is typically the moment when the parent's board of directors has approved the spinoff transaction. This implies that, at the time of the spinoff announcement, the parent has completed enough preliminary work on the expected costs, financing needs, and potential obstacles that might prevent the spinoff, to be confident that the announced transaction can be completed. For example, Gibson Dunn (2018) mention a six-month period for preparations and negotiations of the spinoff before its public announcement. In other words, the preparation period for a spinoff is about six months (i.e., from $t-6$ months to t). Nonetheless, the initial consideration of the divestiture would likely occur *before* the preparation of the spinoff (i.e., more than six months prior to the spinoff public announcement). The exact initial consideration date is private information that only insiders have access to, and consequently difficult to verify. Access

to private information can lead to concerns about potential insider trading activities. For example, Charoenwong et al. (2016) find evidence of insider trading one year prior to a spinoff announcement. This suggests that information about the forthcoming spinoff may be available to insiders as early as twelve months before its public announcement (i.e., from $t-12$ months to t).

Because creditors are key players in spinoff transactions and are involved in the preparation of the divestiture, it is likely that private lenders (i.e., banks) have access to private information within the same time frame (i.e., twelve months before the public announcement). Further, borrowers may be willing to share this private information with their lenders, as the proprietary cost is likely low due to the existence of confidentiality agreements between lenders and borrowers. This expectation is corroborated by the findings of Plumlee et al. (2015) that banks access non-public information regarding forthcoming patents of borrowers well in advance of their public announcements. Figure 1 illustrates the timeline of a spinoff transaction. Note that in this study we are interested in the period *before* the formal public announcement of the spinoff.

In the syndicated loan setting, debt-financing characteristics, such as loan-contracting features (interest rate, loan amount, loan maturity, covenants, and performance-pricing provisions) are a function of information asymmetry between lenders and borrowers (e.g., Leland and Pyle 1977; Holmström and Tirole 1997). Lead banks are assigned with reducing information asymmetry, since they assume a delegated monitoring role in lending agreements (Diamond 1984). Specifically, before deciding on loan issuances, banks perform due diligence on borrowers by assessing their publicly available information, yet they also access their *private* information, through an internal communication channel. Using this channel, banks collect information on borrowers' potential to generate future cash flows and estimate their default risk. Because private communication is not directly observable, researchers usually investigate the extent to which banks rely on this information in shaping loan contracting.

Carrizosa and Ryan (2017) identify two mechanisms through which banks obtain private information: (1) projected pro-forma financial statements, and (2) monthly historical financial

statements. Further, they show that the communication of private information is associated with enhanced lender monitoring. Analyzing the consequences of private communication between lenders and borrowers, Roberts and Sufi (2009) reveal that such communication is positively associated with both the likelihood and outcomes of loan renegotiations, Balasubramanyan et al. (2019) document that the quality of privately acquired information is associated with significantly higher lead bank loan retention and lower interest rate spreads, while Bushman et al. (2010) find a positive association with price discovery in secondary loan markets. According to Plumlee et al. (2015), banks access private information regarding forthcoming patents of borrowers in the six-month period before their public announcement. As a result, banks reduce loan spreads for firms with pending patents, with the effect increasing with the value of the patent. Cheng et al. (2019) show that banks demand private information directly from the borrowers' external auditors to facilitate their monitoring efforts. Along similar lines, Baylis et al. (2017) study the role of auditors in lender acquisition of private information about borrowers and conclude that auditor verification of borrower compliance with financial covenants enhances efficient loan contracting. Additionally, Agarwal and Hauswald (2010) find that the exchange of private firm information is contingent upon the physical distance between the borrower and bank, while Gong and Luo (2018) document that private information obtained from borrowers' major customers facilitate more timely and precise evaluation of borrowers' creditworthiness. Overall, to reduce information uncertainty and mitigate perceived credit risk, borrowers have incentives to provide non-public information to lenders regarding their prospects through private communication (Zhang 2008; Hall and Lerner 2010).

The effect of spinoffs on divesting firms is likely contextual. Specifically, spinoffs generally result in improved operational performance and decreased information asymmetry of the resulting parent and spun-off firm (Schipper and Smith 1983; Krishnaswami and Subramaniam 1999; Desai and Jain 1999). In a debt-contracting context, however, a spinoff can also lead to potential wealth transfers from creditors to shareholders or new creditors. While the firm value- and transparency-

enhancing effects of spinoffs are commonly agreed upon (e.g., Veld and Veld-Merkoulova 2008; Lee and Madhavan 2010), there is conflicting evidence on the effect of spinoffs on bondholders. For example, Parrino (1997) and Maxwell and Rao (2003) detect important wealth transfers from bondholders to shareholders after spinoffs. Hite and Owers (1983) and Dittmar (2004) find that spinoff announcements have an insignificant effect on bond returns, while Veld and Veld-Merkoulova (2008) show a positive effect of spinoffs on bond returns.

Given that upcoming spinoff announcements are generally not expected by the public (Augustin et al. 2020), banks can only access corporate divestiture information by making use of their private communication channel with firm managers. Similar to Plumlee et al. (2015), we expect that private information on a forthcoming spinoff is available to banks before public spinoff announcements. Based on the evidence of informed trading in the twelve-month period before the spinoff announcement (Charoenwong et al. 2016), banks may also be informed of the forthcoming spinoff up to one year before its public announcement. If the value- and transparency-enhancing effects of spinoffs dominate, banks are likely to perceive lower default risk and reward borrowers accordingly. While we acknowledge the potential for a contrasting effect due to wealth transfers, given the inherent differences between bondholders and banks, we consider it a less likely outcome. Banks are less likely to suffer from negative wealth transfers due to their comparative advantages in accessing borrowers' private information relative to investors in the bond market who rely mostly on publicly available information (Fama 1985). Additionally, we consider wealth transfers to new creditors when the newly spun-off entity would issue debt using the transferred assets as collateral. This circumstance is also less likely to occur, as banks commonly include covenants in loan contracts that prohibit unapproved transfer of collateral. Having access to borrower inside information mitigates pre-contract information uncertainty and post-contract monitoring problems (Bharath et al. 2008; Denis and Mihov 2003; Rajan 1992). Overall, this leads to the expectation that banks incorporate private information regarding a forthcoming spinoff in loan contracting.

Nonetheless, we acknowledge arguments that would weaken the probability of such an effect. For example, banks' access to the borrowing firm information does not exclude the possibility – inherent to any agency setting (Jensen and Meckling 1976; Fama and Jensen 1983; Christensen et al. 2016) – that the borrowing firm attempts to opportunistically secure more favorable loan contracting terms by providing abnormally positive estimates of future cash-flows. Moreover, banks are likely to use information on forthcoming spinoffs only if it is provided in a *timely* manner by borrowing firms. Research documenting no reaction from market participants before spinoff announcements (Veld and Veld-Merkoulova 2008) could indicate that they do not pick up pre-spinoff adjustments in firms' interest rates. However, the high debt-market relevance of the spinoff decision coupled with banks' ability to attain information about the likelihood of the divestiture suggests that they do access and use the information regarding impending spinoffs in loan pricing.

Finally, we consider the potential for the inclusion of a “material adverse change” (MAC) clause in the loan contract. The MAC would allow the lender to demand the repayment of debt or to let the spinoff proceed and modify the terms of the contract. Nonetheless, even though MAC clauses are a valuable tool of *ex-post* adjustments in response to unforeseen events, they are almost never invoked in loan contracting (Sufi 2009). This could be due to the difficulty in proving the unforeseen nature of adverse events and thus the difficulty in legal enforcement of such clauses (Ivashina and Scharfstein 2010). Overall, we formulate the following hypothesis (stated in the null form):

HYPOTHESIS 1a. *Banks do not charge higher or lower spreads on loans to spinoff firms relative to firms without spinoffs in the one-year pre-spinoff announcement period.*

In addition to *ex-ante* estimating the likelihood of the transaction, we also examine if banks are able to estimate the implications of the divestiture (on the divesting firm) before its public announcement. Specifically, we assess if banks are likely to adjust loan pricing depending on borrowers' *ex-post* change in riskiness. If lenders are able to estimate that the spinoff will increase (decrease) the riskiness of certain borrowers, they will likely increase (decrease) loan spreads for

these high-risk (non-high-risk) firms relative to other non-divesting firms. We therefore expect incrementally higher (lower) spreads in the pre-spinoff announcement period for borrowers undergoing a high-risk spinoff (non-high-risk spinoff). A high-risk spinoff refers to a spinoff transaction that causes a significant deterioration in the divesting firm’s credit risk. We formulate the following hypothesis (in alternate form):

HYPOTHESIS 1b. *Banks charge incrementally higher (lower) spreads on loans to firms with high-risk spinoffs (non-high-risk spinoffs) relative to firms without spinoffs in the one-year pre-spinoff announcement period.*

3. Research Design

We test our predictions by building on the specifications used in the loan-contracting literature (e.g., Bharath et al. 2008; Bharath et al. 2011). Specifically, we use equation (1) to test if banks have inside information regarding forthcoming spinoffs in the 365-day period before their public announcements, and if they include such information in determining loan prices.

$$Spread_t = \delta_0 + \delta_1 PreSpinoff1Year_t + \delta_2 Borrower-Specific Controls_{t-1} + \delta_3 Loan-Specific Controls_t + Lead Lender, Year, and Industry Fixed Effects + \varepsilon_t \quad (1)$$

where *Spread* represents the “all-in-drawn” spread over LIBOR for syndicated loans, as reported by Dealscan; *PreSpinoff1Year* is an indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement, and zero otherwise.

To assess the incremental effect of the post-spinoff changes in risk on the spreads charged on loans extended in the one-year period before a spinoff announcement, we replace *PreSpinoff1Year* with *PreSpinoff1YearHighRisk* and *PreSpinoff1YearNon-HighRisk* in equation (1). *PreSpinoff1YearHighRisk* (*PreSpinoff1YearNon-HighRisk*) is an indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to high-risk (non-high-risk) spinoff firms, and zero otherwise. High-risk (non-high-risk) spinoffs are those where the decrease in Altman’s Z-score from the one-year pre-spinoff period to the one-year post-

spinoff period is (not) in the 75th percentile of the decreases computed for all the firms in the same two-digit SIC industry and year.

$$\begin{aligned}
 Spread_t = & \delta_0 + \delta_1 \text{ PreSpinoff1YearHighRisk}_t + \delta_2 \text{ PreSpinoff1YearNon-HighRisk}_t \\
 & + \delta_3 \text{ Borrower-Specific Controls}_{t-1} + \delta_4 \text{ Loan-Specific Controls}_t \\
 & + \text{Lead Lender, Year, and Industry Fixed Effects} + \varepsilon_t
 \end{aligned} \tag{2}$$

Our variables of interest in equation (2) are *PreSpinoff1YearHighRisk* and *PreSpinoff1YearNon-HighRisk* because they reflect banks' incorporation of private information regarding future spinoffs in loan-contracting terms (if any) in the 365-day period before the spinoff announcement. A significant coefficient would suggest that the information available to banks *before* the public announcement of spinoffs influences their risk assessment and consequently the determination of interest rates.

We include both lagged *Borrower-Specific Controls* and *Loan-Specific Controls* in equations (1) and (2) (e.g., Bharath et al. 2008, 2011). We include *Borrower-Specific Controls* such as *Firm Size*, as the cost of borrowing has been shown to be negatively associated with firm size (e.g., Blackwell et al. 1998). Further, we control for *ROA*, *Loss*, and *Negative Equity* because lenders offer lower interest rates to more profitable and solvent firms (Kim, Tsui, and Yi 2011). Further, we add *Current Ratio*, as firms' ability to meet their short-term obligations is negatively associated with the cost of borrowing. We further control for credit risk using *Leverage* (Jensen and Meckling 1976) and an indicator variable, *Investment Grade*, that indicates whether the Standard & Poor credit rating of the borrower is in the investment grade category (Bharath et al. 2008).² Further, we expect the cost of borrowing to be negatively associated with the presence of tangible assets (*Tangibility*) (e.g., Kim, Song, and Zhang 2011; Florou and Kosi 2015).

² For firms with missing credit ratings, we generate a synthetic rating based on the approach of Doumplos et al. (2015) by estimating the following equation: $Credit\ Rating_t = \beta_0 + \beta_1 (Pretax\ income/Total\ assets_{t-1}) + \beta_2 (EBIT/Interest\ expense_{t-1}) + \beta_3 (Common\ equity/Total\ assets_{t-1}) + \beta_4 (Common\ equity/Long\ term\ debt_{t-1}) + \beta_5 (Natural\ logarithm\ of\ total\ assets_{t-1}) + Year\ and\ industry\ fixed\ effects + \varepsilon_t$.

As *Loan-Specific Controls*, we include the natural logarithm of the amount of a loan facility (*Facility Amount*), the natural logarithm of loan maturity measured in months (*Maturity*), the total number of lenders in each loan facility (*NLenders*), and the total number of financial covenants of a loan facility (*NCovenants*). We include these variables to control for the joint determination of loan-contracting terms (Kim, Song, and Zhang 2011). Further, we use an indicator variable for whether the loan facility is secured (*Secured Loan*). We control for loan type with an indicator variable equal to one if the loan is a term loan, and zero otherwise (*Term Loan*), and for loan purpose with an indicator variable equal to one if the loan has a refinancing purpose, and zero otherwise (*Refinancing Loan*). We include *Relationship Lending*, defined as an indicator variable that takes the value of one if a borrower obtained a loan from the current lead lender(s) in the last five years, and zero otherwise (Bharath et al. 2011; Ivashina 2009). Finally, we include year and industry fixed effects to control for time effects and time-invariant industry effects.³ We also control for time-invariant lead arranger level confounders by including lead lender fixed effects. Please see Appendix 2 for detailed definitions of all variables.

To mitigate the effect of outliers, we winsorize all continuous variables at the 1% and 99% levels. For ease of interpretation, we *standardize* all continuous variables with zero mean and unit variance. In all our estimations, we cluster standard errors at the borrower level.⁴

Further, we describe our selection of variables that we use in cross-sectional analyses. To gauge the incremental effect of the *ex-post change in reporting quality*, we employ five proxies for reporting quality: (1) positive (i.e., income-increasing) total abnormal accruals based on Kothari et al. (2005); (2) positive (i.e., income-increasing) abnormal working capital accruals based on McNichols (2002); (3) two comprehensive metrics of real earnings management activities as in Cohen and Zarowin (2010), namely, the sum of abnormal discretionary expenses multiplied by

³ In all regressions we use one-digit SIC codes. Our inferences are robust to controlling for industry fixed effects based on the two-digit SIC codes.

⁴ In untabulated analyses, we alternatively double cluster at both year and borrower levels and obtain consistent inferences.

negative one and abnormal production costs and the sum of abnormal cash flows and abnormal discretionary expenses, both multiplied by negative one; (4) the granularity of segmental disclosures; and (5) net operating assets scaled by lagged total assets. We define *Increase Reporting Quality* as an indicator variable equal to one if borrower reporting quality improves from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. We consider that reporting quality improves in the post-spinoff period if the positive abnormal accruals, real earnings management, or net operating assets (segmental disclosure) decrease (increases). For control firms, we compute the changes in reporting quality between one-year pre-loan initiation and one-year post-loan initiation. We add *Increase Reporting Quality*, its interactions with *PreSpinoff1YearHighRisk* and *PreSpinoff1YearNon-HighRisk*, and a control for low reporting quality at loan initiation (*Low ExAnte Reporting Quality*) to model (2).

We use several proxies to measure *Reporting Complexity*. Specifically, *# Words* is the count of all words in a 10-k filing. *# Unique Words* is the count of words occurring at least once in a 10-k filing. *# Characters* is the total number of characters in the 10-k filing. *# Tables* is the total number of tables in a 10-k filing. *# Days between fiscal year-end and filing date* captures the lag (and hence the complexity) in financial reporting. We define *Decrease Reporting Complexity* as an indicator variable equal to one if borrowers' reporting complexity (i.e., # words, # unique words, # characters, # tables or # days between fiscal year-end and filing date) decreases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. For control firms, we compute the changes in reporting complexity between one-year pre-loan initiation and one-year post-loan initiation. In this estimation, we add the following variables to model (2): *Decrease Reporting Complexity*, its interactions with *PreSpinoff1YearHighRisk* and *PreSpinoff1YearNon-HighRisk*, and a control for high reporting complexity at loan initiation (*High ExAnte Reporting Complexity*).

To reflect *Operating Complexity*, we employ the number of business segments and foreign earnings. *Decrease Business Complexity* is an indicator variable equal to one if the borrower

business complexity (i.e., the number of business or geographic segments, or the proportion of foreign income) decreases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. For control firms, we compute the changes in number of segments and foreign income between one-year pre-loan initiation and one-year post-loan initiation. We augment model (2) by adding *Decrease Business Complexity*, its interactions with *PreSpinoff1YearHighRisk* and *PreSpinoff1YearNon-HighRisk*, and a control for the degree of operating complexity at loan initiation (*ExAnte Business Complexity*).

Finally, to assess the effect of the *type* of spinoffs on loan pricing, we replace *PreSpinoff1YearHighRisk* and *PreSpinoff1YearNon-HighRisk* with four indicator variables capturing the loans extended to high-risk (non-high-risk) borrowers undergoing a focusing (non-focusing) spinoff. We consider a borrower to go through a focusing spinoff if the parent and the spun-off entity operate in different primary two-digit SIC industries.

4. Data and Sample

We use a sample of loan facilities provided to U.S. firms during the 1986-2017 period. We obtain data on all loan facilities available in the Dealscan database. Subsequently, we use the link file from Chava and Roberts (2008) to merge the Dealscan file with financials from Compustat. We follow Bharath et al. (2011) and use only accounting information that is publicly available at the time the loan is granted.⁵

We exclude loan facilities of non-U.S. firms and those with missing information on loan-specific characteristics. We also exclude facilities of financial services firms (SIC codes between 6000 and 6999) because these firms are subject to different disclosure and regulatory requirements. Further, we eliminate facilities with missing financials, those provided to firms from industries with fewer than five observations, and loans without a lead lender (following Ivashina (2009) to identify

⁵ Specifically, if the loan start date is six months or later than the fiscal year end of year t , we use the accounting data of that fiscal year t . If the loan start date is less than six months after the fiscal year end of year t , we use the accounting data from the fiscal year $t-1$.

the lead lender). This process results in a sample of 50,619 loan facilities (*Final Sample*). Table 1 presents the sample-selection process.

Next, we obtain spinoff data from the SDC Platinum database. We consider only the first spinoff event by any of the divesting firms (Bergh and Sharp 2015).⁶ Following Augustin et al. (2020), we focus on spinoff announcements for which the spinoffs were subsequently completed or withdrawn. In other words, we discard spinoffs whose status is “unknown,” “intended,” or “rumored.”⁷ We identify 259 facilities provided to firms in the 365-day period before their spinoff announcement. For a high-risk spinoff, banks’ willingness to reward the borrower for potential spinoff benefits is likely to be moderated/mitigated by the adverse impact of the spinoff on borrowers’ credit risk. To cleanly identify whether banks recognize and value the operational and/or informational benefits from spinoffs, we distinguish between spinoff events depending on whether or not the parent firms experience significant *ex-post* deterioration in credit risk. To gauge the *ex-post* impact of a spinoff on credit risk, we use the change in Altman’s Z-score from the one-year pre-spinoff period to the one-year post-spinoff period to proxy for increases in firm financial distress after the spinoff. Thus, we consider a spinoff to be *high-risk* if, after the spinoff, the parent firm experiences a decrease in Altman’s Z-score that is more than the 75th percentile of the yearly decreases in the score computed for all firms available in Compustat within each two-digit SIC code.⁸ Based on this criterion, we identify that 20 out of the 259 loans of spinoff firms have been extended to firms undergoing a high-risk divestiture.⁹

⁶ Inferences do not change if we allow for multiple spinoff events.

⁷ There are 72 facilities extended in the one-year pre-spinoff period whose spinoff status is “unknown,” “intended,” or “rumored.” We currently include these spinoffs in the control sample. However, our inferences remain unchanged if we exclude these 72 observations from our tests.

⁸ Our risk measure captures the extreme increases in default risk in the post-spinoff period relative to industry peers. The rationale is twofold: (1) only material increases in credit risk are likely to be relevant for the lenders and (2) it allows us to consider the level of credit risk before the spinoff announcement, since companies with high *ex-ante* credit risk are less likely to experience the highest increases in default risk.

⁹ We use three alternative definitions of post-spinoff changes in risk and tabulate the results in Table SA1 (see Supplementary Appendix). First, a high-risk spinoff firm is one that experiences a decrease in Altman’s Z-score higher than the percentile 75th or files for bankruptcy in the three-year post-spinoff period. Second, we define a high-risk spinoff as a spinoff where the parent suffers a decrease in Altman’s Z-score that is in the upper tercile (i.e. percentile 67th) of all the decreases in Z-score computed for firms in the same year and two-digit SIC industry. Third, we use the

In Table 2 we present the distribution of our final sample by year and industry. In panel A, we observe a smaller number of observations in the early years, but the coverage increases subsequently. Panel B shows the two-digit SIC classification of the borrowers, indicating a concentration of loans in the manufacturing sector (SIC codes ranging from 2000 to 3999).

5. Results

Descriptive statistics and correlations

Table 3 presents descriptive statistics for all (unstandardized) variables used in our empirical tests. We partition the sample based on *PreSpinoffYear* and test for differences in the means, distributions, and proportions of our variables in the two sub-samples. The results show that, on average, loan facilities extended to spinoff firms in the 365-day period before a spinoff public announcement (*PreSpinoffYear* = 1) have different characteristics compared to the other facilities (*PreSpinoffYear* = 0). Most importantly, *Spread* for facilities granted in the 365-day period before spinoff announcement has a mean value of 166 basis points (median 125 basis points), whereas the mean *Spread* of the other facilities is 225 basis points (median 200 basis points). The difference is statistically significant (t-statistic = 6.46, $p < 0.01$; χ^2 -statistic = 48.77, $p < 0.01$).

More favorable lending terms for the facilities granted 365 days before a spinoff announcement are also apparent in terms of a lower number of financial covenants (mean *NCovenants* of 1 vs. 1.3; median of 0 vs. 1), higher loan amount (mean *Facility Amount* of \$630 million vs. \$306 million), and lower probability of extending a secured loan (mean *Secured Loan* of 0.40 vs. 0.58). Moreover, the facilities granted 365 days before a spinoff announcement involve more participants (mean *NLenders* of 11.13 vs. 7.02) and are more likely to be extended by lead lenders with prior lending relationships (mean *Relationship Lending* of 0.49 vs. 0.38). There are no significant differences in terms of *Term Loan* and *Refinancing Loan*.

percentage change in Altman's Z-score in the one-year post-spinoff period relative to the one-year pre-spinoff period, multiplied by negative one. Inferences are similar when using these alternative definitions of *ex-post* changes in risk.

Further, we observe significant differences in terms of borrower characteristics. Firms that receive a loan facility in the 365-day period before a spinoff announcement are more likely to have an investment-grade rating (mean *Investment Grade* is 0.53 vs. 0.27) and hold more tangible assets (mean *Tangibility* is 0.37 vs. 0.34). They are also larger (mean *Total Assets* of \$138,630 million vs. \$21,152 million), more profitable (mean *ROA* of 3.2% vs. 1.4%), less liquid (mean *Current Ratio* of 1.64 vs. 1.87), and less likely to report a loss (mean *Loss* of 0.17 vs. 0.27) or having negative equity (mean *Negative Equity* is 0.004 vs. 0.07). The firms have similar leverage ratios.

Table 4 reports Pearson correlations. The coefficients above the diagonal correspond to correlations in the sub-sample of facilities granted in the 365-day period before the spinoff announcement (*PreSpinoffYear* = 1), while those below the diagonal correspond to correlations in the sub-sample of other facilities (*PreSpinoffYear* = 0). The correlations indicate similar relations between the variables across the two sub-samples. For instance, we observe that loan spreads are positively correlated with the number of financial covenants, maturity, and likelihood of being a secured or a term loan. Loan spreads decrease when the facility amount is large, more lenders are involved in the deal, loan purpose is refinancing, and there is a prior lending relationship with one of the lead lenders. In terms of borrower characteristics, spreads are positively associated with leverage and liquidity, and negatively correlated with firm size, investment grade status, profitability, and tangibility. As expected, both *Loss* and *Negative Equity* firms receive higher loan spreads, given the higher associated risk.

Main results

In Table 5, we present our main results. Specifically, we examine how upcoming spinoffs relate to loan spreads using four regression specifications. Column (1) of Table 5 shows that the coefficient of *PreSpinoffYear* is negative but insignificant, indicating that, on average, loan spreads are not associated with upcoming spinoffs.

Next, we analyze the incremental effect of the upcoming spinoffs conditional on their effect on divesting firms' credit risk. If banks are able to *ex-ante* distinguish between "good" and "bad"

spinoffs, they will likely incorporate into current loan spreads the information regarding future changes in credit risk. Specifically, in column (2) of Table 5 the coefficient on *PreSpinoff1YearHighRisk* is positive and significant ($\delta = 0.852$, $p < 0.05$), while the coefficient on *PreSpinoff1YearNon-HighRisk* is negative and significant ($\delta = -0.086$, $p < 0.05$). These effects are also economically significant. As we use standardized coefficients, the computation of the economic significance is straightforward: *Spread* has an unstandardized mean of 224.95 and a standard deviation of 147.63 outside the one-year pre-spinoff period. With a standardized coefficient of *PreSpinoff1YearHighRisk* = 0.852 (*PreSpinoff1YearNon-HighRisk* = -0.086), this implies that, all else equal, in the one-year pre-spinoff period the spread of high-risk (non-high-risk) borrowers would increase (decrease) by $0.852 \times 147.63 = 125.781$ ($0.086 \times 147.63 = 12.696$) basis points. In percentage terms, relative to the mean of the unstandardized spread, this corresponds to a $125.781/224.95 = 55.92\%$ increase ($12.696/224.95 = 5.64\%$ decrease). These results indicate that banks are able to foresee post-spinoff credit risk deterioration and charge incrementally higher (lower) spreads for loan facilities granted in the 365-day period before a public spinoff announcement to high-risk (non-high-risk) spinoff firms.

In column (3) of Table 5, we alternatively use *divesting firm fixed effects* to account for within-year invariant factors at the borrower level. This fixed-effects specification absorbs the variation in loan spreads due to unobservable borrower-level time-invariant factors, allowing us to identify the effect of the upcoming spinoff on the spreads of the loans, by holding the borrower constant. If potentially omitted variables related to borrower-level invariant factors drive our results, controlling for borrower fixed effects would therefore make the coefficients of our test variables insignificant. However, the results corroborate our findings from column (2), and suggest that the effects we observe are related to the upcoming spinoff.

Further, to mitigate the possibility that our results are attributable to potential inherent differences in the characteristics of the spinoff and non-spinoff firms, we restrict our sample *only* to the facilities granted to spinoff firms (*Spinoff Sample*). By doing so, we compare the spreads on

loan facilities extended 365 days before the spinoff announcement with the spreads on other facilities granted to spinoff firms more than 365 days before the spinoff announcement. The results reported in column (4) of Table 5 suggest that in the year prior to a spinoff announcement, high-risk spinoff firms pay higher spreads, whereas non-high-risk borrowers are charged lower spreads. This result is consistent with our previous findings that banks are likely informed of the upcoming spinoffs one year before their public announcement, are able to foresee their implications, and adjust loan spreads accordingly in the pre-spinoff period.

The estimated coefficients of the control variables in Table 5 are generally consistent across estimations and with prior research. Specifically, banks require higher loan spreads on loans extended to more leveraged and loss-making firms. Further, loan spreads are negatively associated with the number of financial covenants, the amount and maturity of the loan facility, and the number of lenders involved in the syndicated loan. In addition, the coefficients indicate that the existence of a prior lending relationship with a lead lender, refinancing purpose, investment grade status, size, profitability, and liquidity ratio are associated with lower spreads.

Robustness tests

Instrumental variable analysis

To address the potential for reverse causality and correlated omitted variables, we use an IV approach. Specifically, we use the likelihood that past spinoffs of industry peers were successful (i.e., industry peers that have undertaken a spinoff in the previous two years have positive returns). The rationale behind our instrument is that industry peers' successful spinoffs are associated with the focal firm's decision to conduct a spinoff, since they reflect potential capital market benefits of undertaking such a corporate divestiture. At the same time, rival firms' spinoff decisions do not affect banks' assessment of credit risk, and consequently the spread of loans extended to the firm

in the pre-spinoff period. Table SA2 (Supplementary Appendix) shows that the results are robust to using the IV approach.^{10, 11}

Additional robustness analyses

We perform several robustness tests and present the results in Table SA4 of the Supplementary Appendix. First, we build on Schnabl (2012) and Srivastava (2014) to perform placebo (falsification) analyses. These tests consist of using alternative (placebo) spinoff announcement dates to test the impact of forthcoming spinoffs on loan pricing.¹² The results indicate that the pricing of loan facilities granted two or three years before a public announcement of a high-risk (non-high-risk) spinoff is *not* incrementally higher (lower) relative to the facilities granted to non-spinoff firms. These findings suggest that the effect we document is not due to fundamental characteristics of spinoff firms, but rather is due to banks accessing private information about the upcoming divestiture.

Second, we examine the possibility that parent firms benefit from an *ex-post* reduction in leverage if excessive bondholder debt is assigned to the spun-off firm. We control for the decrease in parent firms' leverage and find that our inferences are not affected by this additional control variable. Third, we assess if lenders provide favorable terms to the parent firms in anticipation of future business with the spun-off firm (cross-subsidization). We find that 16 (i.e., about 6%) of the facilities received by parent firms in the one-year pre-spinoff period were provided by the same lead lenders that grant a loan to the spun-off firm one year after the divestiture. Excluding these loans from the sample does not alter our inferences. Fourth, we consider the possibility that some

¹⁰ The Kleibergen-Paap LM statistic is significant, indicating that the model is not under-identified. Furthermore, the Cragg-Donald Wald F-statistic and the Kleibergen-Paap Wald F-statistic reject the weak identification test. The Anderson-Rubin and the Stock-Wright tests reject the null hypothesis that our instrument is weak.

¹¹ We assess if there is a difference in the access to bank financing in the pre-spinoff announcement period between high-risk and non-high-risk spinoff firms. In Table SA3 (Supplementary Appendix), we find no significant difference between the proportion of high-risk and non-high-risk spinoff firms that issued bank loans in the pre-spinoff announcement period. This result indicates that the success of a corporate spinoff is *not* likely to be determined by the borrowers' access to loan financing prior to the divestiture.

¹² That is, we deliberately move backwards the spinoff announcement date by 365 days (i.e., one year) and 730 days (i.e., two years).

loans in our sample potentially moved from the parent firm to the spun-off entity in the post-spinoff period. We find only 10 out of the 259 loans in our sample that could have been assigned to the spun-off after the divestiture. Specifically, we examine “loan purpose” as reported in Dealscan and identify only four loans that were explicitly issued to the parent in conjunction with the spinoff. Additionally, we exclude six loans that were granted just one week before the spinoff announcement because of their high likelihood of travelling with the spun-off entity. Fifth, our results are robust to excluding 141 loans of spinoff firms with a refinancing purpose as reported in Dealscan, as private information can be gathered during refinancing negotiations (Wachtell et al. 2016).¹³

6. Cross-Sectional Analyses

We next investigate cross-sectional factors that may influence banks’ loan pricing in the 365-day pre-spinoff announcement period. These constructs gauge whether borrowers’ reporting quality, reporting and operational complexity, and spinoff type are relevant to banks when assessing the incremental impact of forthcoming spinoffs.¹⁴

Borrower financial reporting quality

In this section, we assess if there is a loan pricing effect of the *ex-post* change in borrowers’ financial reporting quality. Having a high quality of reporting is instrumental in reducing information asymmetry between lenders and borrowers in a syndicated loan setting (e.g., Armstrong et al. 2010; Christensen et al. 2016). Specifically, the lead lender assesses credit quality by analyzing publicly available information about the borrowers’ performance, future cash flows,

¹³ In additional robustness tests presented in Table SA5 (Supplementary Appendix), we (1) use entropy balancing, (2) employ a robust regression approach (Leone et al. 2019), (3) trim the control sample, in line with Colak and Whited (2007), and (4) add interest coverage to control for default risk and market-to-book to control for growth opportunities. Inferences are similar using these analyses.

¹⁴ The Supplementary Appendix provides an analysis of the effect of focusing versus non-focusing spinoffs (please see section 2 and Table SA6), as well as an examination of the effect of spinoff announcements on financial and non-financial covenants (please see section 3 and Table SA7). In untabulated tests, we detect a significant decrease in the number of segments, abnormal accruals, and net operating assets, and an increase in disclosure quality in the one-year post-spinoff period.

and future risks (Donelson et al. 2017; Cheng et al. 2019). Having access to reliable publicly available accounting information should therefore reduce information asymmetry and mitigate potential adverse selection and moral hazard problems. Consistent with this argument, better financial reporting quality is associated with more favorable debt-contracting terms, such as credit spreads (e.g., Bharath et al. 2008; Costello and Wittenberg-Moerman 2011; Graham et al. 2008).

In a spinoff context, the quality of borrowers' financial information is likely to be highly relevant from a lender perspective, because it aids firm monitoring by external parties in both the pre- and post-divestiture periods. Given the banks' focus on downside risk, we expect that post-spinoff improvements in reporting quality are particularly beneficial for high-risk spinoff firms which could enjoy incremental reduction in loan spreads, despite their overall increase in riskiness. The increased firm transparency would be positively priced as it constitutes a successful divestiture outcome, which likely allows lenders to better assess the performance of the borrowers with improved post-spinoff information environment, reducing costly bank monitoring of high-risk borrowers. Instead, lenders already view non-high-risk spinoffs as "good" divestitures and price their loans accordingly by charging lower spreads. Therefore, it is likely that banks will only marginally reward the improvements in transparency of non-high-risk spinoff firms with incrementally lower loan spreads. In sum, if banks anticipate transparency-enhancing improvements in post-spinoff reporting quality for high-risk spinoff firms, they may charge incrementally lower spreads *before* the public spinoff announcement.

The results in Table 6 show that, while the main coefficients are similar to our main tests in Table 5, the coefficient on the interaction term *PreSpinoff1YearHighRisk x Increase Reporting Quality* (*PreSpinoff1YearNon-HighRisk x Increase Reporting Quality*) is negative and significant (insignificant), regardless of the reporting quality measure used. We find loan spreads to be significantly lower when high-risk borrowers undergoing a spinoff improve their financial reporting quality *ex-post*, while the post-spinoff increase in reporting quality has no differential

effect for non-high-risk borrowers.¹⁵ Overall, given their focus on borrowers' downside risk, lenders seem to foresee and incrementally price the potential post-spinoff improvement in transparency of high-risk spinoff firms.¹⁶

Borrower reporting and operational complexity

We further examine other potential effects of spinoffs: reducing divesting firms' reporting and/or operating complexity. Complex firms are likely confronted with both informational and operational challenges. Managers who need to coordinate multiple and/or unrelated operations may find it difficult to focus on the core line of business. The ensuing operational inefficiencies may result in capital misallocation across different divisions (Rajan et al. 2000), an increased demand for managerial talent (Bushman et al. 2004), and greater advisory requirements (Coles et al. 2008). Further, complex firms require greater research and information-processing capacity from investors, creditors, and analysts relative to firms operating solely in one industry or country. Increased borrower complexity creates information processing difficulties that may result in substantial information asymmetries between borrowers and lenders. Organizational complexity may also increase borrowers' default risk because it is likely associated with operational inefficiencies. While banks are sophisticated players that are well equipped to deal with information asymmetry, substantial effort is still needed to understand complex firms (Chakraborty et al. 2022). We argue that borrowers' complexity increases their default risk and the associated information

¹⁵ In terms of economic significance, pre-spinoff loans issued to high-risk firms that will increase reporting quality have spreads that are between 11.8% (column 1) and 51.3% (column 3) lower relative to the spreads on loans pertaining to non-spinoff borrowers. The calculation of the economic significance based on cross-sectional tests is nonetheless impacted by the small number of observations in the treatment groups. We therefore advise the readers to interpret our findings with caution.

¹⁶ In untabulated tests, we also consider the pre-spinoff reporting quality level as a cross-sectional variable and find that for high-risk companies with low levels of reporting quality at loan initiation, banks charge incrementally lower loan spreads in the pre-spinoff period. For these riskier borrowers with poorer information quality, the expected benefits of spinoffs are likely to be larger. Therefore, if lenders are aware of the ensuing divestiture and perceive it as beneficial for the divesting firms, they are likely to lower loan pricing for this group of borrowers in the pre-spinoff period. In contrast, the effect for the non-high-risk companies is insignificant, suggesting that lenders are particularly focused on borrowers' downside risk when pricing the expected benefits of spinoffs.

processing costs of lenders. As a result, borrower complexity is likely associated with less favorable loan-contracting terms (Chakraborty et al. 2022; Garleanu and Zwiebel 2008; Lou and Otto 2020).

Spinoffs may be positively perceived by banks if they increase the precision of borrowers' publicly available information as well as when they facilitate the understanding of borrowers' operations (Krishnaswami and Subramaniam 1999). Accordingly, banks are likely to price spinoffs favorably resulting in less complex financial reporting or operations. While reducing complexity facilitates bank monitoring, banks may especially reward the divestitures where the post-spinoff improvements in the readability of disclosures and/or operational efficiency mitigate the *ex-post* increase in borrower credit risk (i.e., high-risk spinoffs). This effect is due to banks' asymmetrical focus on borrowers' downside risk when making lending decisions. However, when it comes to non-high-risk spinoff firms, we do not expect that the post-spinoff decrease in complexity will have a significant effect on loan price because these divesting firms already enjoy a spread reduction for the *ex-post* improvement in credit quality. We therefore argue that, when the divestiture has negative credit-risk outcomes, informed lenders may incrementally reward firms with upcoming complexity-reducing spinoffs.

Columns (1) to (5) in Table 7 present the results on the effect of *ex-post* changes in reporting complexity. The standalone coefficients are similar to our main tests in Table 5, yet the coefficient of *PreSpinoff1YearHighRisk x Decrease Reporting Complexity* (*PreSpinoff1YearNon-HighRisk x Decrease Reporting Complexity*) is negative and strongly significant (insignificant) irrespective of the reporting complexity measure used. These results suggest that pre-spinoff loan spreads are incrementally lower when high-risk borrowers exhibit lower reporting complexity in the post-spinoff period.

Columns (1) and (2) of Table 8 show our results for post-spinoff changes in operating complexity. While the standalone coefficients are similar to our main tests in Table 5, the coefficient of *PreSpinoff1YearHighRisk x Decrease Business Complexity* (*PreSpinoff1YearNon-HighRisk x Decrease Business Complexity*) is negative and significant (insignificant) in both

columns. In the pre-spinoff period, banks therefore charge incrementally lower spreads to high-risk firms with a decrease in business complexity. These results suggest that, due to banks' focus on borrowers' downside risk, the pre-spinoff loan spreads are incrementally lower when high-risk borrowers experience a reduction in their reporting or operating complexity subsequent to a spinoff. In this set-up, the increase in *ex-post* credit risk is, at least partly, mitigated by the improvement in the information or operational efficiency.

7. Conclusions

Spinoffs have become increasingly prevalent, as managers and investors have realized the pitfalls of over-diversification. Oft-touted benefits of spinoffs include increased corporate focus, and thus, enhanced valuation transparency for the parent firm. However, spinoffs may also have negative consequences for the divesting firm, such as removal of revenue-generating assets and consequent deterioration in credit risk. We investigate whether, *before* a formal public announcement of the divestiture, banks are able to foresee the implications of spinoffs for the parent firms and incorporate them in their loan pricing.

We find that, while in the pre-announcement year banks charge higher spreads for borrowers with *ex-post* negative spinoff outcomes (i.e., high-risk spinoffs), they charge lower spreads for borrowers with *ex-post* non-high-risk spinoffs. In other words, banks are able to disentangle the value- and transparency-enhancing effects of spinoffs from potential negative consequences and price loans accordingly. We find that the effect is not only statistically significant, but also economically meaningful, with an upcoming high-risk (non-high-risk) spinoff announcement resulting in an on-average increase (decrease) of 126 (13) basis points in loan spreads relative to non-divesting borrowers. We further find that, in the 365-day pre-spinoff period, loan spreads are incrementally lower when borrowers undergoing a high-risk spinoff concurrently exhibit improvements in their reporting quality or reductions in their reporting or operational complexity after the divestiture. This suggests that loan prices incorporate the net effect of the negative and

positive outcomes of spinoffs, since the increase in spread due to a higher *ex-post* credit risk is offset by a decrease in spread associated with the divestiture's positive outcomes. Further, we observe that high-risk spinoffs are penalized by banks when they are structured as non-focusing spinoffs, as these spinoffs likely deliver only marginal benefits.

Our results provide opportunities for future research to investigate if the ability of banks to foresee spinoffs impact the manner in which other market participants – shareholders or bondholders – react to a spinoff announcement when the divesting firm benefits from access to bank loan financing in the pre-spinoff period. Our empirical findings are subject to potential limitations. For example, given the unobservable nature of private communications, we cannot exclude the possibility that banks are able to foresee the probability and implications of impending divestitures due to their superior processing and assessment of publicly available information. Therefore, we advise that our results should be interpreted with caution.

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Appendix 1: Institutional Background on Spinoffs

Spinoffs are corporate divestitures that imply the separation of a firm into two or more independently traded firms. Generally, the divesting parent firm continues trading under the same listing, and the spun-off entity becomes a newly listed stock. The separation results in an allocation of assets and liabilities from the parent to the newly spun-off entity, and consequently in a reduction in the asset base of the original firm (Hite and Owers 1983).

Spinoffs differ from the other types of divestitures on several levels. Both spinoffs and equity carve-outs involve issuance of new shares, but in the former they are distributed to the existing shareholders of the parent firm on a pro-rata basis, instead of selling the shares of a subsidiary to outsiders as in the latter. As a result of the proportional distribution of shares, at inception, the shareholder base in the new firms (parent and spun-off entity) remains unchanged, which may not necessarily be the case in equity carve-outs. Hence, spinoffs give shareholders the opportunity to trade their shares in the parent and the spun-off entity independently. Thus, spinoffs tend to be more beneficial to shareholders relative to other types of divestitures (Bergh and Sharp 2015). Another difference is that equity carve-outs or asset sales involve an infusion of funds into the parent corporation, whereas a spinoff normally does not provide the parent with a cash transfer. Carve-outs or asset sales are often the divestiture methods preferred by financially distressed firms, while generating cash is not usually a primary motivation behind spinoff decisions. Instead, the benefits of spinoffs to the divesting firm are often associated with organizational governance savings and reduced size and complexity (Bergh and Sharp 2015). Additionally, spinoffs are an attractive way to reorganize by many firms because if they are structured appropriately, they do not have any tax implications.

However, spinoffs may also raise concerns about their impact on compliance with existing debt covenants and the allocation of assets and liabilities between the various corporate divisions (Wiebe 2018). Moreover, spinoffs are costly transactions and might involve the loss of positive synergies to joint operations as well as economies of scale in raising external capital (Hite and Owers 1983).¹⁷ Other potential disadvantages relate to stock-market index exclusion, decline in analyst following, or vulnerability to hostile takeovers (Wachtell et al. 2016). The benefits of a spinoff must therefore exceed the associated costs for the divestiture to serve shareholders' interests.

In the U.S., the parent firm's board of directors makes the decision to undertake a spinoff. Shareholder approval is not a formal requirement because these transactions are structured as stock-dividend distributions (Wachtell et al. 2016). As highlighted by Wachtell et al. (2016), decisions about many aspects of the spinoff transaction are taken by the board of directors and management of the divesting parent. These decisions relate to the business units to be divested, the allocation of assets and liabilities to the spun-off entity, the appointment of the board of directors and top management team of the spun-off entity and their compensation, or the spun-off entity's strategic goals and corporate governance mechanisms.¹⁸

¹⁷ The spinoff costs relate to the "registration of the new share certificates, distribution of the new shares, and duplication of the ongoing flow of servicing costs associated with dividend payments, ownership transfers, listing on an organized exchange, etc." (Hite and Owers 1983, 411).

¹⁸ Although initially the decisions regarding the spun-off entity are made by the divesting parent firm, the spun-off firm has the autonomy to make whatever changes it deems fit following the spinoff. Nonetheless, the failure of the spun-off entity could be detrimental also for the divesting parent's shareholders if they choose to retain their shares in the spun-off entity following the initial allocation (Wiebe 2018). Therefore, the duty of the board of the divesting parent is to establish the spinoff terms in a manner that serves the best interests of the parent's shareholders, which means that the allocation of assets and liabilities should ensure that both the new parent and spun-off firm are solvent and financially viable. Several studies conclude that, in the allocation of assets and liabilities to the companies resulting from a spinoff,

Appendix 2: Definitions Of Variables

Main variables

<i>PreSpinoffYear</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement, and zero otherwise (from SDC Platinum).
<i>PreSpinoffYearHighRisk</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to high-risk spinoff firms, and zero otherwise (from Compustat). High-risk (non-high-risk) spinoffs are those where the decrease in Altman's Z-score from the one-year pre-spinoff period to the one-year post-spinoff period is (not) in the 75 th percentile of the decreases computed for all the firms in the same industry and year. Altman's Z-score is computed as follows: $1.20 \times \text{Working capital/Total assets} + 1.40 \times \text{Retained earnings/Total assets} + 3.30 \times \text{ROA} + 0.60 \times \text{Market value of equity/Book value of debt} + 1.00 \times \text{Sales/Total assets}$.
<i>PreSpinoffYearNon-HighRisk</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to non-high-risk spinoff firms, and zero otherwise (from Compustat).

Dependent variable

<i>Spread</i>	The interest rate that a borrower pays in basis points over LIBOR or LIBOR equivalents (spread all-in-drawn from Dealscan).
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Loan-specific variables

<i>Facility Amount</i>	The natural logarithm of the amount of a loan facility (from Dealscan).
<i>Maturity</i>	The natural logarithm of loan maturity measured in months (from Dealscan).
<i>NCovenants</i>	The total number of financial covenants of a loan facility (from Dealscan).
<i>NLenders</i>	The total number of lenders in each loan facility (from Dealscan).
<i>Refinancing Loan</i>	An indicator variable equal to one if the purpose of the loan is refinancing, and zero otherwise (from Dealscan).
<i>Relationship Lending</i>	An indicator variable equal to one if in the last five years the current lead lender granted a loan to the borrower where he was also a lead lender, and zero otherwise (from Dealscan).
<i>Secured Loan</i>	An indicator variable equal to one if the loan is secured, and zero otherwise (from Dealscan).
<i>Term Loan</i>	An indicator variable equal to one if the loan is a term loan, and zero otherwise (from Dealscan).

Borrower-specific variables

<i>Current Ratio</i>	Current assets divided by current liabilities in year $t-1$ (from Compustat).
<i>Firm Size</i>	The natural logarithm of total assets in year $t-1$ (from Compustat).
<i>Investment Grade</i>	An indicator variable equal to one if the credit rating of the borrower in year $t-1$ is at least "BBB-," and zero otherwise (from Compustat).
<i>Leverage</i>	The ratio of total liabilities to total assets in year $t-1$ (from Compustat).
<i>Loss</i>	An indicator variable that equals one if net income is negative in year $t-1$, and zero otherwise (from Compustat).
<i>Negative Equity</i>	An indicator variable equal to one if total assets are lower than total liabilities in year $t-1$, and zero otherwise (from Compustat).
<i>ROA</i>	The ratio of net income to total assets in year $t-1$ (from Compustat).

managers make deliberate financial policy choices that are aligned with shareholders' interests, as the ability to cover debt payments determines the resulting companies' capital structure (e.g., Dittmar 2004; Mehrotra et al. 2003).

Tangibility Net property, plant, and equipment divided by total assets in year $t-1$ (from Compustat).

Variables used in the cross-sectional tests

<i>Decrease Business Complexity</i>	An indicator variable equal to one if the borrower business complexity (i.e., the number of business and geographic segments or the proportion of foreign income) decreases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. For control firms, we compute the changes in number of segments and foreign income between one-year pre-loan initiation and one-year post-loan initiation (from Compustat).
<i>Decrease Reporting Complexity</i>	An indicator variable equal to one if borrower reporting complexity (i.e., # words, # unique words, # characters, # tables or # days between fiscal year-end and filing date) decreases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. For control firms, we compute the changes in reporting complexity between one-year pre-loan initiation and one-year post-loan initiation (from Loughran and McDonald 10X File Summaries).
<i>ExAnte Business Complexity</i>	Either (1) the number of business and geographic segments or (2) the absolute value of the ratio of foreign pretax income to total pretax income at loan initiation (from Compustat).
<i>High ExAnte Reporting Complexity</i>	An indicator variable equal to one if borrower reporting complexity at loan initiation is higher than the industry-year median, and zero otherwise (from Loughran and McDonald 10X File Summaries).
<i>Increase Reporting Quality</i>	An indicator variable equal to one if borrower reporting quality increases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. Reporting quality increases if the positive abnormal accruals, real earnings management, or net operating assets (segmental disclosure) decrease (increases). For control firms, we compute the changes in reporting quality between one-year pre-loan initiation and one-year post-loan initiation (from Compustat).
<i>Low ExAnte Reporting Quality</i>	An indicator variable equal to one if borrower reporting quality at loan initiation is lower than the industry-year median, and zero otherwise (from Compustat).
<i>PreSpinoff1YearHighRiskFocusing</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to high-risk borrowers undergoing a focusing spinoff, and zero otherwise. A spinoff is focusing if the parent and spun-off firm operate in different two-digit SIC code industries, and non-focusing otherwise (from SDC Platinum).
<i>PreSpinoff1YearHighRiskLarge</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to high-risk borrowers undergoing a large spinoff, and zero otherwise. A spinoff is large if the value of the upcoming spinoff transaction scaled by the parent total assets is above the sample median, and small otherwise (from SDC Platinum).
<i>PreSpinoff1YearHighRiskNonFocusing</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to high-risk borrowers undergoing a non-focusing spinoff, and zero otherwise (from SDC Platinum).
<i>PreSpinoff1YearHighRiskSmall</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to high-risk borrowers undergoing a small spinoff, and zero otherwise (from SDC Platinum).
<i>PreSpinoff1YearNon-HighRiskFocusing</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to non-high-risk borrowers undergoing a focusing spinoff, and zero otherwise (from SDC Platinum).
<i>PreSpinoff1YearNon-HighRiskLarge</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to non-high-risk borrowers undergoing a large spinoff, and zero otherwise (from SDC Platinum).
<i>PreSpinoff1YearNon-HighRiskNonFocusing</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to non-high-risk borrowers undergoing a non-focusing spinoff, and zero otherwise (from SDC Platinum).
<i>PreSpinoff1YearNon-HighRiskSmall</i>	An indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement to non-high-risk borrowers undergoing a small spinoff, and zero otherwise (from SDC Platinum).

Variables used in robustness tests (Supplementary Appendix)

<i>Decrease Leverage</i>	An indicator variable equal to one if leverage decreases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise (from Compustat).
<i>Industry Peers Successful SpinoffsHighRisk</i>	An indicator variable equal to one for all loan facilitates extended to firms whose industry peers had past successful spinoffs and experience a decrease in Altman's Z-score from the one-year pre-loan initiation to the one-year post-loan initiation in the 75 th percentile of the decreases computed for all the firms in the same industry and year, and zero otherwise (from Compustat).
<i>Industry Peers Successful SpinoffsNon-HighRisk</i>	An indicator variable equal to one for all loan facilitates extended to firms whose industry peers had past successful spinoffs and do not experience a decrease in Altman's Z-score from the one-year pre-loan initiation to the one-year post-loan initiation in the 75 th percentile of the decreases computed for all the firms in the same industry and year, and zero otherwise (from Compustat).
<i>Interest Coverage</i>	The natural log of ratio $(1 + \text{EBIT}/\text{Interest expenses})$ in year $t-1$ (from Compustat).
<i>Market-to-Book</i>	The ratio of market value of equity to book value of equity in year $t-1$ (from Compustat).
<i>ΔRisk</i>	The percentage change in Altman's Z-score in the one-year post-spinoff period relative to the one-year pre-spinoff period, multiplied by negative one (from Compustat).

TABLE 1
Sample construction

	N
1 Initial sample of loan facilities from Dealscan	372,528
2 Less: Facilities not matched to Compustat (using Dealscan-Compustat Link from Chava and Roberts (2008))	(195,968)
3 <i>Facilities matched to Compustat</i>	<i>176,560</i>
4 Less: Facilities extended to non-U.S. firms	(83,450)
5 <i>Facilities extended to U.S. firms</i>	<i>93,110</i>
6 Less: Facilities without available information on main facility characteristics (spread, # covenants, maturity, amount, # lenders)	(18,818)
7 <i>Facilities with available information on main facility characteristics</i>	<i>74,292</i>
8 Less: Facilities of financial firms	(9,203)
9 Less: Facilities without available financial data	(14,101)
10 Less: Facilities of firms in industries with less than five observations	(6)
11 Less: Facilities without a lead lender	(363)
12 <i>Final Sample</i>	<i>50,619</i>

TABLE 2
Sample distribution

Panel A: Distribution by year

Year	# Loans (total)	# Loans of high-risk spinoff firms	# Loans of non-high-risk spinoff firms	# Other loans
1986	54	0	0	54
1987	507	0	1	506
1988	1,224	0	11	1,213
1989	1,097	0	6	1,091
1990	1,033	0	7	1,026
1991	940	0	4	936
1992	1,092	0	8	1,084
1993	1,381	0	2	1,379
1994	1,639	0	13	1,626
1995	1,537	0	9	1,528
1996	2,157	0	14	2,143
1997	2,764	0	13	2,751
1998	2,349	0	14	2,335
1999	2,202	4	12	2,186
2000	2,297	0	24	2,273
2001	2,241	0	14	2,227
2002	2,233	9	2	2,222
2003	2,171	0	7	2,164
2004	2,395	0	7	2,388
2005	2,294	0	9	2,285
2006	2,038	0	9	2,029
2007	2,062	1	5	2,056
2008	1,079	1	3	1,075
2009	780	0	1	779
2010	1,257	0	6	1,251
2011	1,694	0	1	1,693
2012	1,493	0	6	1,487
2013	1,748	3	9	1,736
2014	1,653	2	10	1,641
2015	1,487	0	9	1,478
2016	1,377	0	3	1,374
2017	344	0	0	344
Total	50,619	20	239	50,360

Panel B: Distribution by industry

Two-digit industry	Description	# Loans (total)	# Loans of high-risk spinoff firms	# Loans of non-high-risk spinoff firms	# Other loans
01	Agricultural Production – Crops	155	0	0	155
02	Agricultural Production – Livestock	10	0	0	10
07	Agricultural Services	30	0	0	30
10	Metal, Mining	167	0	6	161
12	Coal Mining	162	0	4	158
13	Oil & Gas Extraction	2,645	0	5	2,640
14	Nonmetallic Minerals, Except Fuels	122	0	2	120
15	General Building Contractors	36	0	0	36
16	Heavy Construction, Except Building	249	0	0	249
17	Special Trade Contractors	153	0	0	153
20	Food & Kindred Products	1,691	0	14	1,677
21	Tobacco Products	71	0	1	70
22	Textile Mill Products	526	0	1	525
23	Apparel & Other Textile Products	623	0	0	623
24	Lumber & Wood Products	256	0	1	255
25	Furniture & Fixtures	404	0	0	404
26	Paper & Allied Products	800	2	7	791
27	Printing & Publishing	789	0	2	787
28	Chemical & Allied Products	3,032	0	24	3,008
29	Petroleum & Coal Products	446	0	1	445
30	Rubber & Miscellaneous Plastics Products	871	0	0	871
31	Leather & Leather Products	128	0	0	128
32	Stone, Clay, & Glass Products	389	0	0	389
33	Primary Metal Industries	867	0	0	867
34	Fabricated Metal Products	1,069	3	1	1,065
35	Industrial Machinery & Equipment	2,912	2	13	2,897
36	Electronic & Other Electric Equipment	2,799	0	18	2,781
37	Transportation Equipment	1,642	0	9	1,633
38	Instruments & Related Products	2,181	0	12	2,169
39	Miscellaneous Manufacturing Industries	487	0	0	487
40	Railroad Transportation	252	0	6	246
41	Local & Interurban Passenger Transit	83	0	0	83
42	Trucking & Warehousing	426	0	2	424
44	Water Transportation	263	0	0	263
45	Transportation by Air	482	0	0	482
46	Pipelines, Except Natural Gas	134	0	0	134
47	Transportation Services	138	0	3	135
48	Communications	2,511	0	23	2,488
49	Electric, Gas, & Sanitary Services	4,167	9	23	4,135
50	Wholesale Trade – Durable Goods	1,476	0	3	1,473
51	Wholesale Trade – Nondurable Goods	1,068	4	4	1,060
52	Building Materials & Gardening Supplies	154	0	0	154

53	General Merchandise Stores	610	0	2	608
54	Food Stores	514	0	0	514
55	Automotive Dealers & Service Stations	375	0	1	374
56	Apparel & Accessory Stores	595	0	1	594
57	Furniture & Homefurnishings Stores	308	0	0	308
58	Eating & Drinking Places	992	0	1	991
59	Miscellaneous Retail	1,355	0	4	1,351
70	Hotels & Other Lodging Places	215	0	1	214
72	Personal Services	251	0	1	250
73	Business Services	4,199	0	13	4,186
75	Auto Repair, Services, & Parking	125	0	0	125
76	Miscellaneous Repair Services	11	0	0	11
78	Motion Pictures	311	0	0	311
79	Amusement & Recreation Services	863	0	10	853
80	Health Services	1,499	0	14	1,485
82	Educational Services	177	0	2	175
83	Social Services	82	0	0	82
87	Engineering & Management Services	981	0	4	977
99	Non-Classifiable Establishments	290	0	0	290
Total		50,619	20	239	50,360

TABLE 3
Descriptive statistics

Variable	<i>PreSpinoffYear</i> = 0				<i>PreSpinoffYear</i> = 1				T-test	Kruskal Wallis test	Proportion test
	N	Mean	Median	Std. Dev.	N	Mean	Median	Std. Dev.			
<i>Spread</i>	50,360	224.955	200.000	147.634	259	165.606	125.000	130.150	6.46***	48.77***	
<i>NCovenants</i>	50,360	1.335	1.000	1.534	259	1.023	0.000	1.425	3.26***	10.17***	
<i>Facility Amount</i> (\$ millions)	50,360	305.800	100.000	525.700	259	630.100	280.000	821.000	-9.87***	62.03***	
<i>Maturity</i> (months)	50,360	47.515	56.000	24.628	259	44.784	49.000	25.022	1.78*	2.49	
<i>NLenders</i>	50,360	7.016	5.000	7.346	259	11.131	8.000	10.016	-8.97***	40.88***	
<i>Relationship Lending</i>	50,360	0.376	0.000	0.484	259	0.490	0.000	0.501			-3.79***
<i>Secured Loan</i>	50,360	0.580	1.000	0.493	259	0.402	0.000	0.491			5.82***
<i>Term Loan</i>	50,360	0.287	0.000	0.452	259	0.263	0.000	0.441			0.86
<i>Refinancing Loan</i>	50,360	0.557	1.000	0.497	259	0.544	1.000	0.499			0.41
<i>Investment Grade</i>	50,360	0.273	0.000	0.445	259	0.529	1.000	0.500			-9.21***
<i>Total Assets</i> (\$ millions)	50,360	21,152.164	705.291	386,283.518	259	138,629.534	4,327.845	1,186,000	-4.78***	113.42***	
<i>ROA</i>	50,360	0.014	0.033	0.121	259	0.032	0.036	0.093	-2.40**	3.99**	
<i>Leverage</i>	50,360	0.631	0.621	0.264	259	0.624	0.652	0.176	0.46	1.09	
<i>Current Ratio</i>	50,360	1.867	1.556	1.247	259	1.643	1.343	1.178	2.88***	15.90***	
<i>Tangibility</i>	50,360	0.338	0.278	0.244	259	0.371	0.324	0.222	-2.16**	8.59***	
<i>Loss</i>	50,360	0.267	0.000	0.442	259	0.170	0.000	0.376			3.52***
<i>Negative Equity</i>	50,360	0.071	0.000	0.258	259	0.004	0.000	0.062			4.22***

Notes: This table presents the descriptive statistics for our final sample partitioned based on *PreSpinoffYear*, which is an indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement, and zero otherwise. *Facility Amount* is the amount of a loan facility in \$ millions. *Maturity* is the loan maturity measured in months. *Total Assets* is total assets in \$ millions in year *t-1*. All the other variables are defined in Appendix 2. The last three columns show the t-statistics, χ^2 -statistics and z-statistics of the tests whose null hypothesis is that the two sub-samples have identical means, distributions or proportions. Significance level is indicated by *** (for $p < 0.01$), ** (for $p < 0.05$), and * (for $p < 0.10$).

TABLE 4
Correlations

<i>PreSpinoffYear</i> = 0 \ <i>PreSpinoffYear</i> = 1	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
(1) <i>Spread</i>		0.12	-0.37	0.13	-0.24	-0.07	0.53	0.39	0.10	-0.33	-0.16	-0.28	0.16	-0.002	-0.05	0.28	0.06
(2) <i>NCovenants</i>	0.02		-0.06	0.12	0.19	0.04	0.27	0.07	0.34	-0.31	-0.24	-0.11	0.003	0.02	-0.22	0.31	-0.001
(3) <i>Facility Amount</i>	-0.34	-0.05		0.02	0.59	0.22	-0.37	-0.11	0.21	0.48	0.73	0.16	0.13	-0.27	0.13	-0.28	-0.09
(4) <i>Maturity</i>	0.02	0.10	0.21		0.09	0.15	0.20	0.32	0.06	-0.19	-0.01	0.12	0.03	-0.02	0.01	-0.02	-0.03
(5) <i>NLenders</i>	-0.29	0.07	0.58	0.13		0.19	-0.20	-0.03	0.22	0.24	0.38	0.08	0.18	-0.18	0.08	-0.01	-0.06
(6) <i>Relationship Lending</i>	-0.16	-0.003	0.25	0.02	0.19		-0.06	0.10	0.18	0.01	0.20	0.16	0.23	-0.09	0.04	-0.20	0.06
(7) <i>Secured Loan</i>	0.46	0.29	-0.26	0.16	-0.17	-0.10		0.32	0.12	-0.46	-0.28	-0.25	0.13	0.01	-0.10	0.36	0.08
(8) <i>Term Loan</i>	0.32	0.05	-0.06	0.28	-0.04	-0.03	0.24		0.12	-0.21	-0.03	0.0001	0.09	0.02	0.04	-0.01	0.10
(9) <i>Refinancing Loan</i>	-0.04	0.31	0.24	0.14	0.19	0.20	0.10	0.02		-0.06	0.14	0.07	0.19	-0.16	-0.06	0.02	0.06
(10) <i>Investment Grade</i>	-0.42	-0.18	0.40	-0.11	0.31	0.10	-0.46	-0.16	-0.02		0.60	0.19	0.10	-0.30	0.14	-0.38	-0.07
(11) <i>Firm Size</i>	-0.29	-0.17	0.76	0.10	0.49	0.23	-0.33	-0.03	0.17	0.55		0.13	0.26	-0.36	0.19	-0.27	-0.11
(12) <i>ROA</i>	-0.30	-0.001	0.20	0.08	0.13	0.07	-0.20	-0.05	0.01	0.21	0.17		-0.07	-0.17	0.03	-0.64	-0.31
(13) <i>Leverage</i>	0.17	-0.04	0.11	0.06	0.08	0.07	0.12	0.11	0.10	-0.08	0.15	-0.28		-0.64	0.24	-0.02	0.32
(14) <i>Current Ratio</i>	0.01	0.05	-0.18	0.01	-0.15	-0.08	0.06	-0.01	-0.10	-0.14	-0.25	0.08	-0.47		-0.35	0.18	-0.07
(15) <i>Tangibility</i>	-0.11	-0.07	0.14	-0.01	0.09	0.04	-0.12	-0.06	0.02	0.16	0.16	-0.003	0.10	-0.33		-0.19	0.13
(16) <i>Loss</i>	0.33	0.03	-0.18	-0.04	-0.14	-0.07	0.24	0.08	0.02	-0.26	-0.17	-0.67	0.25	-0.06	-0.01		0.14
(17) <i>Negative Equity</i>	0.18	0.01	-0.02	0.04	-0.04	-0.01	0.14	0.09	0.03	-0.15	-0.05	-0.25	0.65	-0.14	-0.001	0.24	

Notes: This table presents the Pearson pairwise correlations for our final sample partitioned based on *PreSpinoffYear*, which is an indicator variable equal to one for all loan facilities granted in the 365-day period before the spinoff announcement, and zero otherwise. Coefficients above the diagonal correspond to correlations in the sub-sample where *PreSpinoffYear* = 1 (N = 259), whereas coefficients below the diagonal correspond to correlations in the sub-sample where *PreSpinoffYear* = 0 (N = 50,360). All the other variables are defined in Appendix 2. Correlations in bold reflect 10% significance.

TABLE 5
The effect of spinoff announcements

Variables	Dep Var: <i>Spread</i>			
	Overall Spinoff Effect	High-Risk vs. Non-High-Risk Spinoffs		
	Final Sample Lead Lender FE	Final Sample Lead Lender FE	Final Sample Firm FE	Spinoff Sample Lead Lender FE
	(1)	(2)	(3)	(4)
<i>PreSpinoff1Year</i>	-0.016 [-0.23]			
<i>PreSpinoff1YearHighRisk</i> (a)		0.852** [2.01]	0.733* [1.74]	0.757* [1.74]
<i>PreSpinoff1YearNon-HighRisk</i> (b)		-0.086** [-2.18]	-0.109** [-2.29]	-0.082* [-1.72]
<i>NCovenants</i>	-0.027*** [-4.72]	-0.027*** [-4.66]	-0.043*** [-5.93]	0.002 [0.06]
<i>Facility Amount</i>	-0.177*** [-18.73]	-0.177*** [-18.73]	-0.181*** [-15.10]	-0.251*** [-6.26]
<i>Maturity</i>	-0.055*** [-9.45]	-0.054*** [-9.43]	-0.051*** [-7.79]	0.025 [1.36]
<i>NLenders</i>	-0.036*** [-6.49]	-0.037*** [-6.54]	-0.060*** [-8.73]	-0.002 [-0.13]
<i>Relationship Lending</i>	-0.055*** [-6.07]	-0.055*** [-6.04]	-0.087*** [-9.08]	-0.066* [-1.69]
<i>Secured Loan</i>	0.445*** [38.81]	0.444*** [38.76]	0.372*** [24.16]	0.427*** [7.52]
<i>Term Loan</i>	0.390*** [40.48]	0.390*** [40.67]	0.356*** [33.32]	0.320*** [8.59]
<i>Refinancing Loan</i>	-0.106*** [-10.48]	-0.107*** [-10.53]	-0.112*** [-9.24]	-0.088** [-2.06]
<i>Investment Grade</i>	-0.273*** [-17.63]	-0.274*** [-17.67]	-0.131*** [-6.03]	-0.208*** [-3.33]
<i>Firm Size</i>	-0.036*** [-3.14]	-0.036*** [-3.14]	-0.013 [-0.54]	0.044 [1.20]
<i>ROA</i>	-0.046*** [-6.80]	-0.046*** [-6.81]	-0.073*** [-7.40]	-0.074 [-1.37]
<i>Leverage</i>	0.080*** [10.34]	0.080*** [10.35]	0.060*** [4.92]	0.120*** [2.72]
<i>Current Ratio</i>	-0.013** [-2.17]	-0.013** [-2.15]	-0.024*** [-2.73]	0.042 [1.39]
<i>Tangibility</i>	-0.001 [-0.22]	-0.001 [-0.21]	0.011 [0.65]	0.064** [2.36]
<i>Loss</i>	0.203*** [13.64]	0.203*** [13.66]	0.126*** [6.80]	0.153* [1.76]

<i>Negative Equity</i>	-0.014	-0.015	-0.044	0.193
	[-0.51]	[-0.52]	[-1.17]	[1.17]
Constant	0.031	0.033	0.077	-0.654***
	[0.39]	[0.41]	[1.30]	[-2.90]
Test for differences in coefficients				
F-test p-value: (a) = (b)		0.03	0.05	0.05
Year FE	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
Industry FE	<i>Yes</i>	<i>Yes</i>	<i>No</i>	<i>Yes</i>
Lead lender FE	<i>Yes</i>	<i>Yes</i>	<i>No</i>	<i>Yes</i>
Firm FE	<i>No</i>	<i>No</i>	<i>Yes</i>	<i>No</i>
Observations	50,619	50,619	50,619	2,281
Adjusted R ²	0.553	0.553	0.601	0.633

Notes: This table presents the results of four model specifications. We use two alternative samples – *Final Sample* (columns (1) - (3)) and the sample of facilities granted to spinoff firms (*Spinoff Sample*, column (4)). All variables are defined in Appendix 2. Coefficients on our variables of interest are presented in bold when statistically significant. The models include year, borrower industry, and lead lender fixed effects (columns (1), (2), and (4)) and year and firm fixed effects (column (3)). The dependent variable in all the models is *Spread*. We cluster standard errors by borrower id. T-statistics are reported in brackets. We also report the p-value from a Wald test assessing the difference in the effect of spinoffs for high-risk and non-high-risk borrowers. Significance level is indicated by *** (for p<0.01), ** (for p<0.05), and * (for p<0.10).

TABLE 6
The effect of financial reporting quality

Variables	Dep Var: <i>Spread</i>					
	<i>Reporting Quality</i>					
	Positive Abn. Acc.	Positive Abn. Work. Cap. Acc.	Real Earnings Management		Disclosure Quality	Bloated Balance Sheet
			1	2		
(1)	(2)	(3)	(4)	(5)	(6)	
<i>PreSpinoff1YearHighRisk x Increase Reporting Quality (a)</i>	-1.097** [-2.56]	-1.139*** [-2.65]	-1.729*** [-4.21]	-1.501*** [-3.28]	-1.319*** [-2.97]	-1.365*** [-3.08]
<i>PreSpinoff1YearNon-HighRisk x Increase Reporting Quality (b)</i>	-0.175* [-1.88]	-0.003 [-0.03]	0.137 [1.35]	-0.066 [-0.71]	0.031 [0.38]	0.024 [0.30]
<i>PreSpinoff1YearHighRisk (c)</i>	0.917** [2.17]	0.907** [2.14]	0.948** [2.33]	1.019** [2.54]	1.124*** [2.86]	1.144*** [2.90]
<i>PreSpinoff1YearNon-HighRisk (d)</i>	-0.064 [-1.49]	-0.091** [-2.18]	-0.108** [-2.52]	-0.083* [-1.93]	-0.096** [-2.02]	-0.094* [-1.87]
<i>Increase Reporting Quality</i>	-0.043*** [-3.66]	-0.061*** [-5.10]	-0.041*** [-4.03]	-0.054*** [-5.51]	-0.038*** [-3.84]	-0.001 [-0.09]
<i>Low ExAnte Reporting Quality</i>	0.071*** [5.65]	0.059*** [4.75]	0.054*** [5.18]	0.069*** [6.72]	0.011 [1.04]	0.017* [1.70]
<i>NCovenants</i>	-0.027*** [-4.67]	-0.027*** [-4.66]	-0.027*** [-4.67]	-0.027*** [-4.65]	-0.027*** [-4.59]	-0.027*** [-4.68]
<i>Facility Amount</i>	-0.177*** [-18.81]	-0.177*** [-18.75]	-0.178*** [-18.93]	-0.177*** [-18.82]	-0.177*** [-18.73]	-0.177*** [-18.75]
<i>Maturity</i>	-0.054*** [-9.34]	-0.054*** [-9.33]	-0.054*** [-9.36]	-0.053*** [-9.31]	-0.054*** [-9.41]	-0.054*** [-9.40]
<i>NLenders</i>	-0.037*** [-6.52]	-0.036*** [-6.47]	-0.037*** [-6.52]	-0.037*** [-6.53]	-0.037*** [-6.55]	-0.037*** [-6.57]

<i>Relationship Lending</i>	-0.055***	-0.055***	-0.055***	-0.055***	-0.055***	-0.056***
	[-6.05]	[-5.99]	[-6.09]	[-6.08]	[-6.00]	[-6.12]
<i>Secured Loan</i>	0.442***	0.442***	0.442***	0.441***	0.443***	0.443***
	[38.60]	[38.59]	[38.70]	[38.59]	[38.74]	[38.64]
<i>Term Loan</i>	0.390***	0.389***	0.390***	0.389***	0.389***	0.389***
	[40.74]	[40.69]	[40.72]	[40.71]	[40.66]	[40.59]
<i>Refinancing Loan</i>	-0.106***	-0.106***	-0.107***	-0.107***	-0.106***	-0.107***
	[-10.50]	[-10.48]	[-10.55]	[-10.56]	[-10.51]	[-10.59]
<i>Investment Grade</i>	-0.273***	-0.272***	-0.271***	-0.271***	-0.274***	-0.272***
	[-17.70]	[-17.62]	[-17.58]	[-17.56]	[-17.66]	[-17.55]
<i>Firm Size</i>	-0.034***	-0.034***	-0.037***	-0.039***	-0.036***	-0.035***
	[-3.04]	[-3.00]	[-3.29]	[-3.39]	[-3.15]	[-3.07]
<i>ROA</i>	-0.047***	-0.046***	-0.045***	-0.044***	-0.046***	-0.046***
	[-6.97]	[-6.83]	[-6.66]	[-6.54]	[-6.78]	[-6.86]
<i>Leverage</i>	0.080***	0.080***	0.080***	0.079***	0.080***	0.081***
	[10.35]	[10.30]	[10.34]	[10.15]	[10.36]	[10.40]
<i>Current Ratio</i>	-0.013**	-0.013**	-0.013**	-0.013**	-0.013**	-0.013**
	[-2.28]	[-2.21]	[-2.20]	[-2.26]	[-2.15]	[-2.16]
<i>Tangibility</i>	-0.001	-0.001	-0.002	-0.001	-0.001	-0.002
	[-0.22]	[-0.15]	[-0.23]	[-0.14]	[-0.22]	[-0.30]
<i>Loss</i>	0.204***	0.203***	0.203***	0.201***	0.203***	0.204***
	[13.69]	[13.64]	[13.70]	[13.54]	[13.68]	[13.75]
<i>Negative Equity</i>	-0.015	-0.015	-0.013	-0.010	-0.014	-0.014
	[-0.52]	[-0.53]	[-0.46]	[-0.35]	[-0.50]	[-0.50]
<i>Constant</i>	0.031	0.029	0.033	0.035	0.036	0.028
	[0.39]	[0.37]	[0.40]	[0.43]	[0.46]	[0.35]
<hr/>						
Test for differences in coefficients						
F-test p-value: (a) = (b)	0.04	0.01	0.00	0.00	0.00	0.00
F-test p-value: (c) = (d)	0.02	0.02	0.01	0.01	0.00	0.00
<hr/>						
Year and Industry FE	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>

Lead Lender FE	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
Observations	50,619	50,619	50,619	50,619	50,619	50,619
Adjusted R ²	0.554	0.554	0.554	0.555	0.554	0.554

Notes: This table reports the regression results of our cross-sectional analyses examining the impact of *ex-post* changes in borrower financial reporting quality. We proxy reporting quality by: the positive (i.e., income-increasing) total abnormal accruals based on Kothari et al. (2005) (column (1)), the positive (i.e., income-increasing) abnormal working capital accruals based on McNichols (2002) (column (2)), two comprehensive metrics of real earnings management activities as in Cohen and Zarowin (2010) (columns (3) and (4)), the granularity of segmental disclosures (column (5)), and the net operating assets scaled by lagged total assets (column (6)). *Increase Reporting Quality* is an indicator variable equal to one if borrower reporting quality increases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. Reporting quality increases if the positive abnormal accruals, real earnings management, or net operating assets (segmental disclosure) decrease (increases). For control firms, we compute the changes in reporting quality between one-year pre-loan initiation and one-year post-loan initiation. *Low ExAnte Reporting Quality* is an indicator variable equal to one if borrower reporting quality at loan initiation is lower than the industry-year median, and zero otherwise. All the other variables are defined in Appendix 2. Coefficients on our variables of interest are presented in bold when statistically significant. All models include year, borrower industry, and lead lender fixed effects. We cluster standard errors by borrower id. T-statistics are reported in brackets. We also report the p-value from two Wald tests for the difference across the coefficients of interest. Significance level is indicated by *** (for p<0.01), ** (for p<0.05), and * (for p<0.10).

TABLE 7
The effect of financial reporting complexity

Variables	Dep Var: <i>Spread</i>				
	<i>Reporting Complexity</i>				
	# Words	# Unique Words	# Characters	# Tables	# Days between fiscal year-end and filing date
	(1)	(2)	(3)	(4)	(5)
<i>PreSpinoff1YearHighRisk x Decrease Reporting Complexity</i> (a)	-1.668*** [-4.04]	-1.666*** [-4.03]	-1.666*** [-4.02]	-1.674*** [-4.00]	-1.659*** [-4.08]
<i>PreSpinoff1YearNon-HighRisk x Decrease Reporting Complexity</i> (b)	-0.005 [-0.05]	-0.070 [-0.67]	0.044 [0.35]	0.274** [2.03]	0.091 [1.12]
<i>PreSpinoff1YearHighRisk</i> (c)	0.944** [2.31]	0.943** [2.31]	0.937** [2.28]	0.935** [2.25]	0.917** [2.27]
<i>PreSpinoff1YearNon-HighRisk</i> (d)	-0.090** [-2.13]	-0.080* [-1.88]	-0.092** [-2.23]	-0.119*** [-2.93]	-0.110** [-2.40]
<i>Decrease Reporting Complexity</i>	-0.083*** [-6.73]	-0.080*** [-6.66]	-0.049*** [-3.76]	-0.051*** [-4.02]	-0.100*** [-8.88]
<i>High ExAnte Reporting Complexity</i>	0.046*** [3.89]	0.041*** [3.42]	0.011 [0.97]	0.025** [2.03]	0.065*** [5.08]
<i>NCovenants</i>	-0.026*** [-4.51]	-0.026*** [-4.49]	-0.026*** [-4.55]	-0.027*** [-4.62]	-0.026*** [-4.44]
<i>Facility Amount</i>	-0.178*** [-18.82]	-0.178*** [-18.82]	-0.177*** [-18.72]	-0.177*** [-18.74]	-0.176*** [-18.85]
<i>Maturity</i>	-0.054*** [-9.36]	-0.054*** [-9.35]	-0.054*** [-9.42]	-0.054*** [-9.42]	-0.054*** [-9.39]
<i>NLenders</i>	-0.037*** [-6.63]	-0.037*** [-6.62]	-0.037*** [-6.57]	-0.037*** [-6.58]	-0.037*** [-6.66]

<i>Relationship Lending</i>	-0.055*** [-6.03]	-0.055*** [-6.01]	-0.054*** [-5.98]	-0.055*** [-6.10]	-0.054*** [-5.92]
<i>Secured Loan</i>	0.441*** [38.62]	0.442*** [38.61]	0.443*** [38.61]	0.444*** [38.73]	0.439*** [38.63]
<i>Term Loan</i>	0.389*** [40.65]	0.389*** [40.67]	0.389*** [40.61]	0.389*** [40.68]	0.388*** [40.69]
<i>Refinancing Loan</i>	-0.105*** [-10.39]	-0.105*** [-10.43]	-0.106*** [-10.48]	-0.106*** [-10.45]	-0.104*** [-10.29]
<i>Investment Grade</i>	-0.272*** [-17.57]	-0.271*** [-17.55]	-0.273*** [-17.63]	-0.273*** [-17.65]	-0.269*** [-17.42]
<i>Firm Size</i>	-0.038*** [-3.32]	-0.038*** [-3.30]	-0.036*** [-3.16]	-0.037*** [-3.27]	-0.029*** [-2.60]
<i>ROA</i>	-0.045*** [-6.71]	-0.045*** [-6.72]	-0.046*** [-6.82]	-0.046*** [-6.79]	-0.045*** [-6.67]
<i>Leverage</i>	0.081*** [10.40]	0.081*** [10.43]	0.080*** [10.36]	0.080*** [10.35]	0.079*** [10.30]
<i>Current Ratio</i>	-0.012** [-2.12]	-0.013** [-2.16]	-0.013** [-2.14]	-0.013** [-2.17]	-0.012** [-2.00]
<i>Tangibility</i>	-0.001 [-0.17]	-0.001 [-0.21]	-0.001 [-0.21]	-0.001 [-0.22]	-0.001 [-0.22]
<i>Loss</i>	0.203*** [13.67]	0.204*** [13.70]	0.204*** [13.68]	0.203*** [13.65]	0.201*** [13.55]
<i>Negative Equity</i>	-0.016 [-0.56]	-0.016 [-0.58]	-0.015 [-0.54]	-0.015 [-0.54]	-0.016 [-0.57]
Constant	0.026 [0.33]	0.029 [0.37]	0.030 [0.38]	0.031 [0.39]	0.020 [0.25]
Test for differences in coefficients					
F-test p-value: (a) = (b)	0.00	0.00	0.00	0.00	0.00
F-test p-value: (c) = (d)	0.01	0.01	0.01	0.01	0.01
Year and Industry FE	Yes	Yes	Yes	Yes	Yes

Lead Lender FE	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
Observations	50,619	50,619	50,619	50,619	50,619
Adjusted R ²	0.554	0.554	0.554	0.554	0.555

Notes: This table reports the regression results of our cross-sectional tests on the effect of *ex-post* changes in borrower financial reporting complexity. We employ five different proxies of reporting complexity based on the Loughran and McDonald 10X File Summaries: (1) the count of all words in the 10-k filing, (2) the count of words occurring at least once, (3) the total number of characters, (4) the total number of tables, and (5) the number of days between the fiscal year-end and the filing date. *Decrease Reporting Complexity* is an indicator variable equal to one if borrower reporting complexity (i.e., # words, # unique words, # characters, # tables or # days between fiscal year-end and filing date) decreases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. For control firms, we compute the changes in reporting complexity between one-year pre-loan initiation and one-year post-loan initiation. *High ExAnte Reporting Complexity* is an indicator variable equal to one if borrower reporting complexity at loan initiation is higher than the industry-year median, and zero otherwise. All the other variables are defined in Appendix 2. Coefficients on our variables of interest are presented in bold when statistically significant. All models include year, borrower industry, and lead lender fixed effects. We cluster standard errors by borrower id. T-statistics are reported in brackets. We also report the p-value from two Wald tests assessing the difference across the coefficients of interest. Significance level is indicated by *** (for p<0.01), ** (for p<0.05), and * (for p<0.10).

TABLE 8
The effect of business complexity

Variables	Dep Var: <i>Spread</i>	
	<i>Business Complexity</i>	
	# Segments	Foreign Income
	(1)	(2)
<i>PreSpinoff1YearHighRisk x Decrease Business Complexity (a)</i>	-1.066** [-2.42]	-1.460*** [-4.28]
<i>PreSpinoff1YearNon-HighRisk x Decrease Business Complexity (b)</i>	-0.036 [-0.45]	0.029 [0.25]
<i>PreSpinoff1YearHighRisk (c)</i>	1.016** [2.41]	1.244*** [3.99]
<i>PreSpinoff1YearNon-HighRisk (d)</i>	-0.079 [-1.64]	-0.091** [-2.20]
<i>Decrease Business Complexity</i>	0.018 [1.19]	-0.071*** [-5.64]
<i>ExAnte Business Complexity</i>	0.001 [0.72]	-0.007 [-1.21]
<i>NCovenants</i>	-0.027*** [-4.68]	-0.026*** [-4.54]
<i>Facility Amount</i>	-0.177*** [-18.76]	-0.177*** [-19.00]
<i>Maturity</i>	-0.054*** [-9.39]	-0.054*** [-9.35]
<i>NLenders</i>	-0.037*** [-6.55]	-0.037*** [-6.52]
<i>Relationship Lending</i>	-0.055*** [-6.01]	-0.054*** [-5.94]
<i>Secured Loan</i>	0.444*** [38.75]	0.441*** [38.63]
<i>Term Loan</i>	0.390*** [40.67]	0.389*** [40.68]
<i>Refinancing Loan</i>	-0.107*** [-10.54]	-0.105*** [-10.42]
<i>Investment Grade</i>	-0.274*** [-17.67]	-0.276*** [-17.79]
<i>Firm Size</i>	-0.038*** [-3.35]	-0.030*** [-2.69]
<i>ROA</i>	-0.046*** [-6.78]	-0.045*** [-6.65]
<i>Leverage</i>	0.080*** [10.36]	0.081*** [10.38]
<i>Current Ratio</i>	-0.013** [-2.13]	-0.013** [-2.30]

<i>Tangibility</i>	-0.001 [-0.08]	-0.004 [-0.64]
<i>Loss</i>	0.203*** [13.64]	0.207*** [13.82]
<i>Negative Equity</i>	-0.014 [-0.50]	-0.016 [-0.56]
Constant	0.022 [0.27]	0.042 [0.53]
Test for differences in coefficients		
F-test p-value: <i>(a) = (b)</i>	0.02	0.00
F-test p-value: <i>(c) = (d)</i>	0.01	0.00
Year and Industry FE	<i>Yes</i>	<i>Yes</i>
Lead Lender FE	<i>Yes</i>	<i>Yes</i>
Observations	50,619	50,619
Adjusted R ²	0.554	0.554

Notes: This table presents the regression results of our cross-sectional tests on the effect of *ex-post* changes in borrower business complexity. We measure complexity by (1) the number of business and geographic segments and (2) the absolute value of the ratio of foreign pretax income to total pretax income. *Decrease Business Complexity* is an indicator variable equal to one if the borrower business complexity (i.e., the number of business and geographic segments or the proportion of foreign income) decreases from the one-year pre-spinoff period to the one-year post-spinoff period, and zero otherwise. For control firms, we compute the changes in number of segments and foreign income between one-year pre-loan initiation and one-year post-loan initiation. *ExAnte Business Complexity* is either the (1) number of business and geographic segments or (2) the absolute value of the ratio of foreign pretax income to total pretax income at loan initiation. All the other variables are defined in Appendix 2. Coefficients on our variables of interest are presented in bold when statistically significant. All models include year, borrower industry, and lead lender fixed effects. We cluster standard errors by borrower id. T-statistics are reported in brackets. We also report the p-value from two Wald tests assessing the difference across the coefficients of interest. Significance level is indicated by *** (for p<0.01), ** (for p<0.05), and * (for p<0.10).

Figure 1 Illustrative timeline of a spinoff transaction (please see separate file)