



Due Diligence

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Are you selling a business or some other form of property? If so, due diligence will likely contribute to the success of your sale. Due diligence reveals material facts, allows for risk mitigation, and ensures buyers and sellers are adequately informed throughout the course of a transaction¹. This is primarily accomplished through the review of financial, legal, environmental, and other relevant records.

The motivation for a buyer to perform due diligence is evident—to ensure that an asset is legal, financially sound, and generally beneficial before it is acquired. While the seller may not share this motivation, they also benefit from the process. The seller’s potential motivators include, but are not limited to:

- Identifying and resolving issues before the buyer discovers them.
- Evaluating potential buyers, their future plans, and how the asset contributes to those plans. This information can strengthen the seller's position during negotiations.

The scope of due diligence is broad; therefore, it is important for the seller to be prepared for the buyer's requests for information. Items the buyer will want to examine include, but are not limited to:

- Financial records
- Intellectual property
- Marketing
- Liabilities
- Human resources
- Sales data
- Operations and infrastructure

Depending on the nature of the transaction, this process can take several months or more. To prepare, the seller can take a couple steps before engaging with the buyer²:

1. Carefully review all documentation to determine what the seller needs to share with the buyer and identify any gaps.
2. Collect this documentation in a manner that is easily accessible for both the seller and buyer.

Typically, the seller in a business acquisition is smaller than the buyer and may not have the expertise to conduct due diligence on their own. In such a case, the seller can utilize a third party (such as Freer Consulting) for guidance through the due diligence process. The seller can engage assistance at any step, or for the process as a whole.

¹ See William J. Gole and Paul J. Hilger, *Due Diligence: An M&A Value Creation Approach* (Hoboken: John Wiley & Sons, 2009) 8-10.

² Jennifer Novotny and Mike Silverman, “Protecting a Seller in the Face of a Buyer’s Due Diligence Investigation”, accessed June 7, 2017, <https://exitpromise.com/protecting-business-seller-due-diligence-investigation>

Freer Consulting assists with due diligence in a number of ways:

- Acts as a liaison with the buyer's legal team, facilitating open communication between the buyer and seller throughout the transaction.
- Performs a comprehensive assessment of the seller and identifies action items to address any informational gaps that require correction.
- Assists the seller with the aforementioned corrections to ensure they are prepared for any requests for documentation from the buyer.
- Responds to specific requests from the buyer (for example, additional documentation, status reports, and other information the buyer needs).

Identification of Relevant Documents

The first step in the due diligence process is to identify any documentation that a buyer may request prior to the sale. It is important to be as thorough as possible, because all business aspects may be considered. While financial data is of obvious interest to a buyer, other records are also significant and should not be neglected.

For example, a seller's operations may make it subject to certain environmental regulations. In the event of a sale, the buyer will assume responsibility for compliance with these regulations. Therefore, the buyer will want to know what its responsibilities will be and if any corrective actions are required either prior to or following the sale. Information useful to the buyer in this case includes:

- Permits (such as stormwater, wastewater, air emissions, etc.) under which the seller is covered.
- Documentation of any control measures the seller employs to maintain compliance with applicable regulations.
- Maintenance records of any relevant equipment or infrastructure.
- Laboratory analysis data, if required by regulatory authorities.
- Notices of noncompliance with regulations and documentation of corrective actions the seller took in response.
- Documentation of any legal actions, such as consent decrees, lawsuits, etc.

Anticipating and identifying what information a buyer will need shortens the sale process and gives the seller the opportunity to address any gaps³.

Tracking and Collating Information

Once relevant documents have been identified, they should be tracked and collated. It is possible that some information will be missing. Proper document tracking enables the seller to quickly see what is missing and take measures to find it. This can be done with spreadsheet software or with more sophisticated methods of document control (e.g., a database). Tracking information should include:

³ See also "Buying a Business: Due Diligence Checklist", Findlaw, accessed June 7, 2017, <http://smallbusiness.findlaw.com/starting-a-business/buying-a-business-due-diligence-checklist.html>

- A list of the documents being tracked and collected.
- The status of the documents (available, not available, pending, etc.).
- Who is responsible for each document.
- The date when each document is finalized.
- Management approval.

Once all documents are available, they should be collected and placed in a single location (a file server, dedicated filing cabinet, etc.) to be readily provided to the buyer.

Handling Additional Buyer Requests

During the due diligence process, the buyer may request information that the seller did not anticipate. This can result in a time-consuming, and potentially unnecessary, search. In this instance, a third-party contractor can serve as a liaison between the buyer and the seller. The contractor can, for example, review existing seller documents to determine if they already have the information the buyer is requesting. It is possible that a buyer will ask for information that is not relevant or applicable to the seller; the contractor can help determine what is needed and what is not. In the event that additional information is needed that the seller does not have, the contractor can facilitate the search for this information, its collection, and its conveyance to the buyer.

In sum, proper due diligence helps ensure that a business sale proceeds as smoothly as possible and on terms that are mutually beneficial for the buyer and the seller.

If you would like to know more about how Freer Consulting can help you conduct due diligence, contact us at (206) 285-9044 or at info@freerconsulting.com.