

## The importance of due diligence when acquiring a business

The due diligence process can be perceived as expensive, time consuming and pedantic. So, is it a valuable part of the acquisition process or a necessary evil? Due diligence provides a vital confirmation of the accuracy of the accounts on which a bid is based. However, the importance of the due diligence process goes far beyond this. Due diligence also covers the identification and avoidance of risk, whilst providing a sound base from which to plan the post-deal integration strategy.

### TYPES OF DUE DILIGENCE

**Financial due diligence** focuses on the past, present and future, including:

- an in-depth analysis of underlying historical performance, cash flow generation, assets and liabilities;
- a summary of the key strengths and weaknesses of the business and an analysis of its key products, services and employees;
- a review of the underlying financial systems and controls;
- management and employee considerations;
- an analysis of the company's taxation position, highlighting potential liabilities and risks; and
- a detailed review of the company's financial projections, including comment on the reasonableness of the principal assumptions, key sensitivities and the principal differences in projected and historical results.

**Legal due diligence** provides:

- comfort on the ownership of assets;
- highlights potential issues arising from past transactions and contractual commitments; and
- analysis of any legal disputes and non-compliance with the law and regulations.

**Commercial due diligence** is more focussed on the future, highlighting:

- the risks inherent in the business model (arising from the customer base, supply chain, etc.);

- assumptions underlying marginal forecasts;
- the prevailing economic environment and the impact this may have; and
- details of the market and competitors.

**Environmental due diligence** investigates:

- whether the business has been meeting legislation compliance levels;
- any potential liabilities arising from the entity's activities; and
- the impact of European environmental legislation.

The potential liabilities arising from environmental issues serve to underline the importance of this area.

In our experience, it is essential that all advisers work closely so as to:

- avoid duplication of work;
- ensure that matters identified which affect other areas of due diligence are effectively communicated; and
- ensure timetables are adhered to.

It is also essential that prior to the commencement of due diligence, all information relevant to the assignment has been compiled and that the vendors (to include key management and directors) have freed up time from the running of the business to be involved in the due diligence process, thereby ensuring a cost efficient and effective buying process.

## DUE DILIGENCE AND NEGOTIATION

Increasingly, due diligence is no longer the final step taken in an acquisition but forms part of the negotiation process itself. Acquirers are using it to negotiate both price and structure. Due diligence is also complementary to the negotiation of vendor representations and warranties.

## HAZLEWOODS LLP CORPORATE FINANCE

Hazlewoods is an acknowledged leader in the provision of due diligence services having previously been voted Specialist Due Diligence Provider at the M&A Awards. We have an expert, dedicated team providing a full range of financial and taxation due diligence services to both corporate and financial investors. We provide partner led support throughout the transaction process, from pre-deal evaluation through to completion and post-deal support

For further information, or to arrange a free initial meeting, please contact:

Paul Fussell

Partner

t: 01242 680000

e: paul.fussell@hazlewoods.co.uk



**PAUL FUSSELL**

Partner

01242 680000

paul.fussell@hazlewoods.co.uk



Staverton Court, Staverton, Cheltenham, GL51 0UX  
Tel. 01242 680000 Fax. 01242 680857

[www.hazlewoods.co.uk](http://www.hazlewoods.co.uk) / @Hazlewoods

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