



Due Diligence

Introduction

Due diligence is the term commonly used to describe the investigation of the affairs of a business or company on behalf of a potential investor, lender or purchaser in advance of completion of a transaction.

Financial due diligence is one part of this investigation, but there are also others, such as legal, commercial and environmental due diligence.

Monahans can assist you with all aspects of financial due diligence.



The Purpose of Due Diligence

The purpose of due diligence work is to enable the prospective purchaser or investor to make an informed decision whether to proceed with the transaction or not.

The objectives of financial due diligence are set out below:

- To confirm information provided by the seller
- To assist negotiation with information discovered;
- To inform the prospective purchaser or investor;
- To confirm the net assets, both title and value;
- To support the price being paid/invested.
- To help set the warranties and indemnities;
- To assess the existence and value of available security.

Public Information



Some information can be gained about the company through public records, such as:

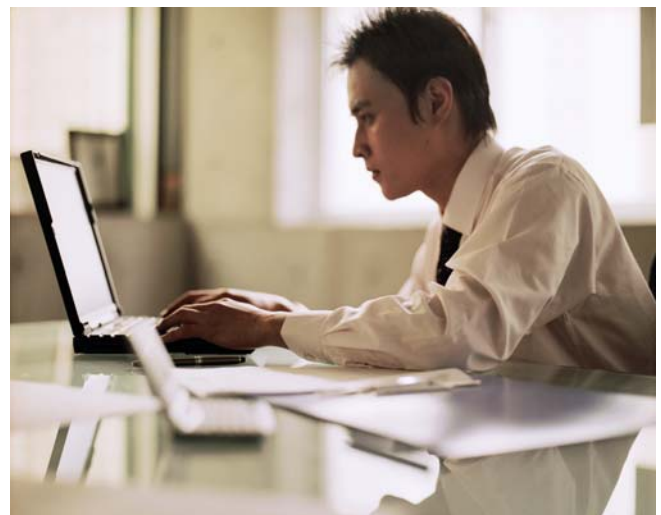
- Registrar of companies – accuracy of statutory records, charges over assets, previous names;
- Proprietary search facilities – industry reviews, company comparisons, credit rating;
- The press – current related events and stories;
- Trade journals – industry and competitor reviews;
- Other, eg DTI reports, credit rating agencies, website and brochures of the target company.

Private Information

The main source of information will be from the company itself. The required information can be derived from access to:

- Accounting records;
- Management information reports;
- Support schedules and analysis;
- Commentaries on performance;
- Marketing reports;
- Minutes of management and directors meetings;
- Statutory books;
- Tax computations;
- Employee files;
- Correspondence files.

Information can also be derived from advisors to the company, such as legal advisors and auditors.



Due Diligence Investigation

A typical full due diligence investigation should cover, but is not limited to, the following areas:

- History of the business;
- Nature and conduct of the trade, including the products or services, major customers, marketing strategy etc;
- Statutory information such as the details of incorporation and company registration number;
- Management and employees, including structure, names, ages and length of service;
- Financial reporting procedures, accounting systems and internal controls, including authority levels, computer security and access controls;
- Accounting policies and any divergence from industry standards;
- Trading results, usually a summary and analysis of three years accounts;
- Net assets, including comparatives to last years results Taxation, as mentioned below;
- Current trading and projections, including budgets and forecasts plus actuals compared to budget;
- Other general matters, eg the premises or insurances.

Depending on the reason for the due diligence exercise, not all of the above may be covered, or it may just be centred on one particular area. The scope of the due diligence will be defined in the engagement terms as agreed prior to the start of the project.

Taxation



Taxation can be costly if things are overlooked. The information arising from the tax due diligence can be very useful to potential purchasers. It will make up the main warranties and indemnities, show opportunities for tax planning and show any residual tax liabilities.

Tax also includes VAT, PAYE and NI, in which any non-compliance can end up in large surcharges, interest and penalties.

Due Diligence Report

The investigating accountant will prepare a due diligence report, based on their findings.

The scope of the engagement will be set out at the beginning of the report as well as any limitations due to unavailable information.

There will be an executive summary which summarises all the relevant findings of the report, so that someone would come to the same conclusion by reading the executive summary as by reading the entire report.

Appendices should be attached to the end of the report and referred to through out. Some typical appendices might be:

- Terms of engagement;
- 2/3 years accounts;
- List of employees and details;
- Organisational chart.



Further Information

Monahans can assist you in all aspects of financial due diligence and assist you with finding contacts for other types of due diligence, such as solicitors. our specialist Corporate Finance Department will be pleased to help.

Please contact **Peter Lugg** in our Bath office on **01225 472800** or email **peterl@monahans.co.uk**