

Due Diligence

One should not buy a company without first learning everything there is to know about that company. That learning process is known as due diligence. During due diligence, a buyer, his accountant, his lawyer and any other professional advisor he employs should examine every aspect of every contract, procedure, relationship, plan, agreement, system, lease, manual and financial document.

The due diligence process requires extraordinary amounts of time and attention so it is best initiated as soon as you, the owner, decide to sell the company. You must first identify the person in your organization who will assemble all of the documents and information your transaction attorneys will require. That employee may have a new full time, albeit temporary job, collecting, researching, and compiling information.

The second benefit of starting the process early is that doing so can help remove any obstacle that might prevent a buyer from traveling a straight path to closing. Keeping the road to closing free from unnecessary impediments compresses the time between the offer and the closing. Time can kill deals.

Once all the documents are collected, your transaction attorneys should update minutes, fill in gaps in stock ownership records and locate minority shareholders and their stock certificates. They should resolve any issue that could stop the buyer cold such as litigation, environmental or statutory violations. Further, they should make the due diligence process as easy as possible for the buyer's advisors. If a seller is required to provide notice or obtain consents from lenders, landlords or various vendors before any transfer can take place, your attorneys should set up the process through which those consents will be obtained.

After your attorneys have combed through every document, they present a comprehensive and well-organized packet of information to a buyer's counsel. The professional presentation of information should: 1) expedite the due diligence process, 2) enhance the seller's credibility with the buyer and 3) enable the buyer's attorneys to stay focused on the transaction. He or she should not be chasing missing documents or asking again for documents that are buried in disorganized boxes.

Finally, early and complete due diligence preparation can help protect the seller from a post-closing lawsuit that could arise from a misrepresentation or breach of warranty. A buyer may demand that the seller make a number of warranties and representations about the company.

Without thorough analysis and consultation with your attorney and management team, how can you warrant, for example, that there is no threatened or pending litigation? Perhaps, hypothetically speaking, a secretary informed your HR director that she had been sexually harassed but the HR director has not yet told you. If you warrant that there is no threatened litigation and this employee subsequently sues the new owner, that new owner can bring suit against you for a breach of warranty. If you do not subject your company to thorough due diligence, you may have a difficult time convincing a jury that you are not liable for this breach.



To help avoid unnecessary detours on the road to closing and to protect yourself afterwards, do your due diligence early and do it thoroughly.

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