CGMA TOOL

M&A due diligence for CFOs part I – buyer: Guidance for small- and mid-sized organisations

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About the tool

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INTRODUCTION

The process of due diligence typically involves a thorough investigation of the business from many different vantage points. The understanding of due diligence is best summarised by *Black's Law Dictionary* as "the diligence reasonably expected from, and ordinarily exercised by, a person who seeks to satisfy a legal requirement or discharge an obligation."

Due diligence usually is thought of as the long list of items the buyer must consider and verify before purchasing a business. It's true that the buyer has a special and enduring duty to thoroughly examine the target company because he or she will have to live with the purchase decision if the deal is completed. It is inexcusable for the buyer and his or her team of advisers to miss obvious and material items relating to the transaction. It is often impossible to verify every detail regarding the target company, but using a team approach with knowledgeable professionals greatly minimises the risk of missing a significant factor. Because it is likely that a few items of risk will miss detection by even the most accomplished buy-side teams, the buyer affords additional protections by carefully crafting the terms of the proposed transaction with items that provide additional security to the buyer.

BUYER'S DUE DILIGENCE

The due diligence effort by the buyer is far more involved than for the seller. The buyer will be raising most, if not all, of the financing for the transaction and will have to satisfy the financial partners that the proposed acquisition is a sound business decision that makes economic sense. Many of the items that compose the buyer's due diligence are being completed concurrently because there typically is a severe time constraint. The first few items listed are the most important, followed by a number of aspects that are, in most cases, equally essential. Generally, the buyer will eventually address all of the issues.

IDENTIFY YOUR ADVISORY TEAM

This is perhaps one of the most important steps the buyer will undertake. Due to the disproportionate risks the buyer faces, the selection of the advisory team is crucial to minimise those risks.

In most instances, the window of opportunity for the buyer to complete its due diligence is sharply restricted. The seller will tolerate an exclusive examination of records and all other applicable factors for a designated period of time. During this phase, the buyer will incur substantial costs and will want an exclusivity understanding with the seller that the business is no longer being actively marketed to other parties. Time is of the essence in this matter. The buyer will have to engage a knowledgeable and experienced team to accomplish all of the due diligence fact finding required within a short time frame.

After the team is assembled, it is essential to lead them into effective analysis.

THE DREAM ACQUISITION

We know of companies actively seeking acquisitions that convene the senior management to think about (dream) the ideal transaction. At this stage, it is appropriate to identify all of the attributes of the ideal acquisition target. This is an important part of buying companies because it helps establish a bar for comparison. There never will be an ideal acquisition, but there are degrees of suitability. Removed from the emotion and momentum artificially imposed on many transactions, having a rationally defined baseline for analysis helps remind the buyer's team of advisers what is really important.

In the meeting, the buyer-side team ranks transaction attributes on a scale of importance to the acquiring firm. Defining these elements in the objective confines of a meeting tends to maintain a pragmatic outlook when a target is within sight. As a potential acquisition candidate is identified, experienced buyers understand that irrational emotions may be disproportionately factored into the process simply because of the excitement of a possible purchase.

IDENTIFY FUNDAMENTALS

Fundamentals are different from the dream attributes. Fundamentals are elements or items that, at a minimum, must be present for consideration. Although they will be different for various buyers, most fundamentals will relate to core interests. The following examples are intended to illustrate a number of common fundamental factors:

- Minimum revenue – Regardless of the other considerations, the target company must be of a certain minimum size to be considered because the due diligence work is substantial.
- Profitable history – Integrating entities following a purchase is difficult enough without the added challenge of turning around the operations of the target. Many buyers will not even consider a target company with weak financial performance.
- Minimum industry ratios – The target company ratios must meet certain minimum levels for the company to be considered. The ratios typically are industry specific and broadly known, or they may be proprietary information maintained by the buyer.

IDENTIFY THE OVERALL STRUCTURE OF THE TRANSACTION

The buyer will have to quickly assess the overall parameters of structuring the transaction. For example, one of the first strategic decisions is whether the offer will be for the assets or the stock of the target company. Additionally, the finance package will have to be determined in short order. If the seller will be requested in part to provide some of the financing, the relative magnitude of this component is very material to the seller.

The overall structure usually is communicated to the seller in a nonbinding letter of intent. Major provisions of the proposed deal are outlined for the seller's review. Major provisions of the transaction are contained in this early communication, with more specific details following.

Define an asset or stock purchase

Basically, there are two ways to acquire a business: buying the assets or acquiring the stock of the target company. There are many fundamental benefits to acquiring the assets of the target company rather than the stock, but knowing the merits of an asset versus a stock transaction is of critical importance. Once the "asset versus stock" decision has been made, negotiations often will focus on tax treatment considerations of the deal structure:

- Asset-based transactions are much more common, particularly among closely held businesses. Asset-based transaction attributes are heavily tipped in favour of the buyer's interests. The most important attributes of asset purchases typically include the ability to get a stepped-up basis in the assets being acquired and the ability to restrict exposure to unknown liabilities attributable to the seller. Asset-based transactions will be considered in detail in a separate chapter.
- Stock-based transactions are less likely because buyers typically are biased against them, as discussed. If a stock-based transaction is considered, it's likely that there are compelling reasons for the buyer. Stock transactions are more common between family members, sales to an Employee Stock Ownership Plan (ESOP) and when the seller has the commanding negotiating leverage to insist on a stock transaction. Stock-based transactions will be considered at length in a separate chapter.

Sources of financing

The buyer has to make some preliminary assumptions about financing the proposed transaction. Typical sources of financing include bank debt, other investor debt or capital, cash flow from the acquisition company, cash flow from the target company and seller financing. Often, the buyer is interested in acquiring the target with as little equity as possible. If the candidate business is acquired entirely with debt, the ability to leverage the existing equity in the acquisition company is substantial. The extent to which debt is used in the acquisition, of course, is very complex and subject to the facts of each proposed transaction:

- **Arranging financing for the transaction from a bank** – In most transactions, some amount of bank financing is part of the deal. Representatives of the bank have to be informed of the transaction details and must be comfortable with the structure. It should be anticipated that for larger amounts, the bank will have to perform its own due diligence and this may be time-consuming. Delays in closing may be caused by the financial institution having to complete due diligence that is more involved than originally intended. The bank will request a pro forma financial statement of the combined entities to feel comfortable that the proposed transaction will provide adequate cash flow to service the higher debt ceiling.
- **Other investors** – Depending on the circumstances, it may be appropriate to find other investors as partners in the acquisition. The target company may have significant interest to another entity making a partnership on the buy side of the transaction attractive. One overriding concern if this strategy is to be successful is deciding where the ultimate control for the transaction resides. It is helpful if there is one controlling investment representing more than 50% of the transaction price; potential complications arise when no single investor has a controlling block.

- **Seller financing** – In most transactions, some percentage of the consideration will be in the form of seller financing. There is, in most instances, an overwhelming bias for the buyer to insist on some amount of seller financing as additional protection that the seller has truthfully disclosed the material attributes and liabilities of the business. The buyer will champion the highest amount the seller will tolerate, and the seller will negotiate for the lowest possible amount. This aspect is vitally important to the seller and the buyer, but the seller has the specter of surrendering the control of the business to the buyer. After the closing is completed, the seller has limited recourse against the buyer if circumstances begin to unravel. From a pragmatic standpoint, the buyer is in a commanding position to control future events after the closing. Finally, the buyer should anticipate the seller demanding collateral for the seller note.
- **Legal documentation** – When financing is provided by a third party such as a financial institution, that party will likely have comprehensive documentation prepared by its own legal counsel, which is singularly oriented to protecting its interests. Loan documentation from a bank often is detailed and is largely directed at protecting the bank in case the borrower's ability to repay the loan is compromised or threatened. The bank will look to every source of possible collateral it can negotiate and attach. In addition to having an interest in specific assets of the borrower, the bank will frequently insist on personal guarantees of principal parties to the transaction. If the seller is providing financing, clearly there is an interest in making sure that the documents, which are generally drafted by the buyer's legal expert, are reviewed by the seller's attorney.

Identify additional areas of negotiation

Typically, a range of the overall consideration for a proposed transaction is decided upon by the buyer before serious negotiations begin. This predetermination of range is helpful as a fall back once negotiations are underway and the forces of deal momentum interject emotion into the transaction equation. A consideration of terms will usually be part of the transactions. Common candidates include the following items:

- **Escrow amount** – An arbitrary amount of the sale proceeds held back by the buyer for a designated period of time.
- **Representations** – The buyer should insist on a representation letter disclosing material items regarding the target company.
- **Consulting agreement** – If applicable, the employment terms extended to the seller are detailed in an agreement that stipulates such things as employee duties, compensation and term of agreement.
- **Earn-out provision** – If applicable, the buyer may extend to the seller the ability to participate in the future success of the acquired company in some defined manner. The earn-out agreement typically represents a quantified amount that the seller may be due depending on the financial performance of the acquired company.
- **Asset allocations** – In asset purchase transactions, the buyer will insist that the seller agree to the buyer's asset allocations.

REVIEW OF LEGAL ISSUES

Parties to a potential transaction will sense the likelihood of a deal moving forward with the anticipation of a completed sale. Typically, the buyer will insist on being in control of the transaction documentation. Being in control in this sense suggests deciding which documents will be produced and being in command of substantially all document production. Each deal is unique, and the document flow will be similarly unique. There are some overall general observations that are worth emphasizing in this very technical high-stakes arena.

- *Controlling the documents and terms of the deal.* An experienced buyer will have an overview of the many facets involved in bringing a transaction to completion. This advanced look into the future is a significant benefit in the negotiating process. Buyers want to control the production of documents simply because "it is my money," and the control of the purse generally dictates this wonderful attribute. Buyers will work with experienced attorneys who are watchful for their client's financial interests.

  Clearly, the preparation of the documents by the buyer's counsel will shade the protective contract language in favor of the buyer. Certainly, the seller's

attorney will review the documents for content and overall equity, but it is difficult psychologically to challenge too many unpopular or questionable provisions without jeopardising the deal. Often many borderline provisions are passed by the seller, but such borderline clauses may have significant advantages to the buyer. Some common marquee documents include the following:

- Confidentiality agreement
- Letter of intent
- Asset or stock purchase agreement
- Corporate resolutions authorizing the transaction
- Seller finance documents, if applicable
- Long-term lease, if applicable
- Noncompetition agreement
- Employment or consulting agreement, if applicable

- **Corporate records** – Verify updates and the current status of items such as the certificate of incorporation, bylaws and corporate minutes.
- **Obtain all necessary consents** – This may be more involved than it first appears. Consider a transaction in which there are several shareholders in the selling company. All of them must eventually agree to the transaction or else the sale will be in jeopardy, if not outright cancelled. Another item may be shareholders in marital property states [jurisdictions], where the consent of all applicable spouses may have to be obtained. Finally, another example is a shareholder currently in the process of a divorce, and suspicions are possibly already very high. Usually, the buyer wants to be in control of this process to ensure that a last-minute withholding of consent does not derail the transaction. Consents may also be required from other stakeholders in the business such as banks, lessors and licence holders.
- **Preparing the "deal book"** – A best practice is the preparation of a deal book, which is the assembly of all related documents accompanying a transaction into a single collection. Specifically, the best deal books are prepared by the buyer's legal counsel, and they are arranged to clearly identify each document with a tab and cross reference to a table of contents. Such a book has the overwhelming attribute of controlling the flow of transaction documents in a single location for ongoing reference. Another advantage is the ability of transaction participants to review the contents for reasonableness and to make adjustments as necessary. There is much less likelihood of last-minute transaction crises if the buyer is well organised in this manner. Deal books are often presented in standard-size binders with a comprehensive index of contents and tabs clearly indicating where the documents are positioned.
- **Perform closing responsibilities** – With most transactions, there are a significant number of legal documents to be executed and completed. Typically, all major agreements have to be verified for accuracy and completeness prior to execution. The purchase and sale agreements often include the following key areas:

  - Transaction description indicating an asset sale or a stock sale.
  - Representations and warranties negotiated by the parties to the transaction. This part of the process has to be very carefully monitored by both parties because such provisions are intended to provide direction and an indication of the process of resolution if issues or questions arise following the closing.
  - The terms of the transaction accompanying the agreement. The terms of the transaction cover, among other areas, financing the deal, possible employment contracts for key individuals and escrow accounts. Very few transactions are for cash, and the payment conditions have to be clearly stipulated. Often the seller is providing a portion of the financing in the form of seller notes, and such aspects of the sale will be carefully reviewed.
  - Transaction covenants and conditions include additional matters such as noncompetition agreements, which are representations that certain actions will be completed or certain activities will be avoided.

REVIEW OF FINANCIAL INFORMATION AND OPERATIONS

The buyer typically will have a tremendous amount of material to consider prior to a closing, and there will be limited time to perform a truly thorough analysis of all the significant matters. It is critical under the time constraints imposed to make sure the transaction team is in place and can react on a timely basis. The length of time allowed for the buyer's due diligence is often expressed in just weeks or days.

This portion of the buyer's due diligence is particularly amenable to review checklists to help ensure that no material items are overlooked. In that spirit, a sample due diligence checklist for the buyer is provided in this chapter. Major areas of review are briefly considered in the following list:

- **Organisational data** – This section includes the verification of the significant data regarding the target company. Included are shareholders and shareholder ownership interests, officers, directors, key managers, legal organisation, affiliate relationships, subsidiaries, divisions, significant legal agreements such as customer contracts and professional advisers.
- **Accounting records** – This includes the financial statements of the target and all other applicable financial records of the business. This list may be very lengthy, but major items at a minimum include financial statements, tax returns, asset ledgers, supporting journals for financial statement accounts, cost accounting systems, inventory schedules, production reporting, accounts payable system, details on all debt, Uniform Commercial Code/ regulatory filing information, fixed asset schedules, depreciation and amortisation schedules, insurance policies, payroll journals, benefit plan information and investment account.
- **Operations review** – This is a thorough analysis of operations to gain a complete understanding of the risk environment. Major items for review include examining business plan; examining supplier contracts; reviewing applicable licences; exploring possible existence of intangible assets such as trademarks, names or copyrights; examining applicable leases and examining labor agreements, management or employment agreements, noncompetition agreements or any other applicable agreements. This also includes a detailed analysis of the operations of the business from major activities to how products are delivered to customers.
- **Contingent liability review** – Consider all potential contingent liability sources. More common sources include potential warranty exposure, correspondence with the corporation's legal counsel, supplier contracts, loan or contract guarantees, royalty or licence arrangements and workman's compensation folders. Confirmation letters to the company's attorney regarding known or pending litigation are recommended.
- **Industry review** – Understanding the industry and the nature of the competition is also an essential step. More common issues include knowing all the major competitors, identifying the strengths and weaknesses of the major competitors, understanding the market potential of all major products and services, verifying emerging industry trends and determining the competitive profile of the target company within the industry. The buyer typically has a thorough understanding of the industry but may not know exactly how the candidate company provides goods and services. Attention to such details is a key to the buyer realizing synergies and economies of scale, if any.
- **Human resources** – This may be the most important aspect of the due diligence. It also is the one area that often is qualitative in nature and most subject to a gut reality check. Some common major concerns include the analysis of the senior management and either the desirability or likelihood of having them continue; understanding the composition of the entire employee base; recognising vacation procedures and possible unpaid vacation liability; determining if there is a union and if there are incentive or bonus programmes in place; determining if there are equity programmes in place such as stock options, phantom stock and stock appreciation rights; determining how the employees are and what health, disability, retirement and life insurance programmes are in place; determining the safety record of the target; determining what critical skills are essential to the business and establishing the historical labour turnover.

- **Environmental issues** – This is listed as a separate item, but it could easily be part of the contingent liability review. Environmental issues are significant because governmental bodies have wide authority to pursue any remedy that is suitable for remediation. The potential exposure is enormous. Clearly, if property is part of the transaction, a thorough analysis of the facility is mandatory. It may be appropriate to complete a level I environmental study almost immediately to quickly uncover any possible deal breakers. If there is any question that there may be significant environmental exposure, the buyer has to seriously question the wisdom of moving ahead with the transaction.

INTEGRATION OF ENTITIES

Once the closing has been completed, the new owner must begin the process of integrating the two entities. Failure to anticipate this vital process is often cited as the primary reason for the failure of the acquisition to attain the anticipated financial benefits for the buyer. The issues related to integrating the entities are vast and include such critical aspects as blending the corporate cultures of the two entities, integrating information and financial reporting systems, coordinating all marketing efforts and understanding how combined product and service capabilities potentially complement one another.

This point specifically is mentioned as a major heading because the failure to adequately anticipate this critical issue is one of the most frequently cited reasons for an acquisition that fails to meet buyer expectations.

Companies that have successfully acquired other businesses probably make the integration of corporate cultures one of their highest priorities.

CLOSING CHECKLIST

This section is included as a summary of all the other documents already discussed, in addition to other matters related to the closing. Typically, there is a transaction quarterback ensuring that all matters related to the closing (of which documents are important aspects) are completed on a timely basis. It is common for a law firm to act as the transaction quarterback for the simple fact that so much of the detail surrounding the sale of the business involves legal documents. The following outline represents items that have been incorporated into successful closings. The range of actions and documents related to closings is vast, and the following outline is representative of the most common activities. Depending on the nature of the transaction, its relative size and the complexity of the negotiations, the actual number of specific actions and documents could be much longer:

	Example actions and documents prior to the closing:
	Confidentiality agreement executed by buyer and seller
	Letter of intent presented to seller
	Buyer presents seller with a preliminary list of due diligence requests
	Buyer and advisers complete due diligence
	Phase I environmental study completed
	Seller's shareholders and board approved the asset purchase agreement
	Buyer obtains commitment for bank financing in part for the transaction
	Seller agrees to terms of seller financing for part of transaction price
	Buyer agrees to terms of seller loan agreement regarding collateral and payments
	Seller agrees to terms of consulting agreement
	Major customers signed a consent to the assignment of an existing supply contract
	Buyer and seller sign asset purchase agreement

	Example closing actions and documents:
	Escrow agreement executed by buyer and seller
	Bank finance documents executed for both acquisition loan and revolver
	Seller loan agreement and seller note executed
	Subordination agreement executed between bank and seller
	Employment agreement for seller executed
	IRS Form 8594 (allocation of purchase price), or other jurisdictional tax forms as required
	Covenant not to compete
	Asset purchase agreement
	Updated authorisations and approvals for the transaction
	Closing or settlement statement

It is a best practice to have an experienced lawyer acting as the closing quarterback. Typically, there are many documents to be executed and distributed, and there is a compelling requirement to have these documents accurately prepared and reviewed. The closing often is in the offices of a lawyer or a financial institution. It is best to anticipate that a few last minute changes will be made to documents and to provide computer access to the professionals charged with getting the documents executed.

BUYER'S DUE DILIGENCE CHECKLIST

The following buyer's due diligence list is intended to be both a learning and an educational tool and not a legal document. The purpose of this checklist is to illustrate a sample, but not necessarily comprehensive, document with the more common issues related to the due diligence process that a buyer of a company should consider. If there is a pending sale of a company, the due diligence will be dependent on the specific facts and circumstances of that transaction. Always engage the services of experienced professionals to assist with the due diligence process.

	Identify advisory team
	Retain experienced transaction legal counsel.
	Retain experienced CPA/Chartered Accountant firm.
	Identify financial resources such as banks, internal funds and personal funds.
	Identify other key advisers such as board members, key managers and partners.

	Structuring the transaction
	Determine if the transaction meets minimum acquisition targets such as revenue, profitability and growth potential. If it does not, explain.
	Determine if the transaction will be an asset or stock purchase.
	Identify how much cash is required at closing.
	Identify what types of warranties and representations will be required.
	Determine how the warranties and representations will be collateralized: escrow account, seller financing, earn-out provisions, consulting or employment agreement or other.

	Financial sources
	Estimate the total consideration to the seller, including all aspects of the transaction.
	Determine what portion of the sale price will be bank financing.
	Determine what portion of the sale price will be internal funds from buyer.
	Determine if funding from other investors is required.
	Determine what amount of seller financing will adequately collateralize the warranties and representations and fill the gap of what will not be in cash at the closing.

	Legal issues
	Generally be prepared to control the production of substantially all of the transaction related documents.
	Common legal documents include: - Confidentiality agreement - Letter of intent - Transaction resolutions - Business intermediary agreement - Asset or stock purchase agreement - Escrow account agreement - Noncompetition and nonsolicitation agreement - Consulting or employment agreement - Financing documents such as seller note and loan agreement - Other agreements and documents as appropriate
	Prepare deal book.
	Obtain all necessary consents.
	Verify all corporate records of the seller.
	Verify responsibilities for closing.

	Organisational data
	Obtain the seller's organisation chart.
	Obtain the seller's ownership schedule including shareholders, affiliates, ownership in affiliates.
	Obtain list of subsidiaries and divisions.
	Obtain the original certificate or articles of incorporation, together with all amendments to date, current bylaws and minutes from board of directors' meetings.
	Obtain a list of locations where the target is qualified to do business.
	Obtain officer and director lists.
	Obtain documentation (if any) for preferred stock, warrants, options or similar securities held by the seller.
	Obtain copies of all significant agreements and contracts: leases, financial documents, property, employment or consulting agreements, vendor agreements, sales agreements and the like.
	Obtain a legal summary of any known environmental liability, product liability, securities matters, contract disputes and the like. In addition, obtain the details of all governmental and other regulatory issues.

	Accounting records
	Obtain three to five years of historic financial statements.
	Obtain budgets, forecasts or business plan.
	Determine how the seller forecasts and plans for future business. If a forecast exists, determine how it compares to results actually attained.
	Review internal controls and determine if those controls are adequate to ensure accurate financial statements.
	Determine if financial statements are prepared by a CPA firm. If they are not, determine if there is a compelling reason to not having the financial statements reviewed by an independent party.
	Obtain details of all reserves, if any.
	Determine if there is any litigation in process. Review all professional service invoices for the past three years.
	Obtain the details of all material off-balance-sheet assets or liabilities.
	Verify title to all assets, especially things like rolling stock (automobiles and trucks) and other major pieces of equipment and machinery. Verify title to all real estate and payment of all applicable real estate taxes, assessments, utilities and so on.
	Identify all computerised accounting and operational functions. Verify the extent computer programs have been modified from standard software programs. Determine if legacy software has been previously installed, making future software integration problematic.
	Verify all taxing jurisdictions and determine whether the seller's tax filings are current.
	Review all tax/regulatory examination reports issued to the seller by taxing jurisdictions and discuss any ongoing examinations.
	Determine if the software systems of the seller are compatible with the software systems of the buyer.

	Operations review
	Identify all product lines, services and revenue producing activities. Analyse such things as the highest volume sources of revenue, the highest profit items, labour intensive products, obsolete products and emerging and promising products for the future.
	If inventories are maintained, verify internal controls and existence of slow moving or obsolete inventory.
	Determine if seller's products and services are proprietary or protected by patents.
	Identify all written agreements or contracts with customers. Verify pricing information and terms of the agreements regarding such things as price increases, assignability and cancellation features.
	Verify if the seller has warranty exposure or if other contingent liabilities pose a significant risk.
	Determine if the seller is subject to any marketing agreements, franchise obligations, joint ventures, buyer agreements or licensing programmes.
	Verify the structure of all marketing and sales functions.
	Verify sales representative's compensation. Verify if sales representatives are employees, manufacturer's representatives or independent contractors. Obtain compensation details for each.
	Verify sales representative's compensation. Verify if sales representatives are employees, manufacturer's representatives or independent contractors. Obtain compensation details for each.
	Examine all pricing policies, cost information, rebates, discounts, return allowances, sales incentives, co-op advertising allowances and the like.
	Determine if outside sales and marketing resources are used and if the seller uses a sales agency.
	Determine how advertising programmes are initiated and funded.
	Identify principal raw materials and other resources to determine security and availability of products.
	Identify any synergies with seller and buyer suppliers and determine if there are opportunities to combine purchases for economies and possible price savings.
	Determine if seller and buyer computer systems are compatible for such basic requirements as inventory records, sales data, service support or production. If they are not compatible, determine the time and cost to have compatible systems.
	Analyse current seller staff levels and determine if they are adequate to manage revenues and customer service levels in the future.

	Contingent liability review
	Examine areas of potential unrecorded claims such as product warranty records, dangerous products and unsafe practices.
	Obtain written representations from owners, officers and the seller's law firm regarding all known or pending disputes.

	Industry review
	Verify industry classification codes (if in multiple lines of business).
	Verify all significant local and national trade associations, and verify if seller is a member or active in any of them.
	Determine if the industries served by the seller are growing and expanding or shrinking relative to the general economy.
	Verify the seller's geographic breakdown of sales and market coverage. Obtain sales data for the most recent years. Check for seasonal or cyclical sales patterns.
	Identify major customers, contact information, annual volume in the major accounts and other pertinent data. Determine if the relationships will likely continue after the close.
	Identify competitive advantages of the seller and weaknesses that contribute to lost revenue.
	Identify the major competitors and the major strengths and weaknesses of each.
	Review industry pricing. Determine if the seller's pricing is competitive. Determine if the seller's operating margins are similar to the industry or significantly different (higher or lower).

	Human resources
	Identify all key managers and verify such items as experience, title, responsibilities, years of service with seller and special attributes.
	Determine if management retention agreements exist (golden parachutes). If so, determine how they are executed and what the financial obligation of the business is.
	Obtain compensation for all employees. Verify the form of compensation: salary, fringe benefits, bonus, profit sharing, equity agreements, stock options, deferred compensation and insurance.
	Determine if current compensation for the employees is competitive with the local market.
	Obtain employment agreements, if any, and verify if any compensation payments are subject to written agreements. Verify the compensation to sales representatives.
	Determine if employees are routinely evaluated. Obtain most recent evaluations.
	Identify all relationships between the seller and other affiliated entities and individuals. Identify all material financial transactions and verify if they are arm's length. Identify any conflicts of interest.
	Identify all employees by location. Within each location, determine if the employees are classified by salary, hourly, part time or another system.
	Determine who processes the payroll.
	Determine if the seller has unionised employees. If so, determine if there have been any strikes or job actions recently and if there are any major issues with the collective bargaining agreement.
	Determine what benefits are maintained by the seller. Verify the existence of retirement plans, medical plans, dental plans, cafeteria plans, expense reimbursement, disability plans and the like.
	Obtain copies of all profit sharing, employee benefit plans, ESOP and pension plans. Determine the existence of defined contribution and defined benefit qualified plans. Verify that there are no unfunded liabilities with any of the qualified ERISA plans.
	Review all Form 5500 (and/or other required regulatory filings) for the past three years.
	Verify compliance with all benefit plans and regulatory agencies
	Compare the seller's benefits with the buyer's benefits for compatibility. Exceptions should be noted in the event the plans are merged.

	Regulatory and environmental issues
	Verify if there are any significant environmental concerns or health and safety issues.
	Obtain reports from any local or national regulatory agencies.

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