**Corporate and Commercial Due Diligence**

This element explains more about what is entailed in corporate and commercial legal due diligence.

**Legal due diligence**

As you have already seen there are a **number of key areas** that a buyer will want typically its advisers to consider in legal due diligence. You will look at some of these key areas in more detail later in this Topic for example, employment, IP& IT, data protection and pensions. The extent to which those areas are considered will depend on, amongst other things, the kind of company, business or assets being acquired, the deal structure and the buyer’s approach to risk.

However, the buyer will also need to consider legal due diligence from a more general corporate and commercial perspective. The scope of the corporate/commercial review will be determined by a variety of factors which might for example, include the sector in which the target company/business operates, its key assets, the time available and the relative bargaining powers of the parties.

**Legal Due Diligence - key corporate areas**

**Constitution of the seller/target**

The buyer will need to check the constitution of the target for a range of reasons. Examples include:

* Checking the target is validly incorporated.
* Checking for any restrictions on the directors' powers or other unusual governance arrangements which could impact the validity of past transactions.
* Establishing whether there are any restrictions (for example, pre-emption rights) on or corporate consents required for the proposed acquisition/ transaction.

The buyer may want to check other areas, examples of which are below, however any problematic provisions can usually be removed or amended post completion. The target company will often adopt new articles to remove problematic provisions or to bring them in line with the buyer or its group companies.

* Considering the different classes of shares and their associated rights.
* Considering whether there are any restrictions in the target’s constitution which would affect the buyer’s plans for the target company.

**Title to shares and/or assets**

The buyer will want to ensure that the seller has good title to:

* the shares in the target company (on a share purchase). For example, have all previous share transfers been properly registered in the statutory books of the target company and have any company buy backs or other changes to the share capital been carried out properly?; and
* the assets being acquired (on an asset sale). For example, is the seller the registered owner of any real estate or registered IP being transferred?

The buyer will also want to check if there are any charges over the shares or assets being acquired.

**Companies House filings and wider corporate governance**

* As well as searching public filings at Companies House to understand more about the target company, for example details of its share capital and information on persons with significant control, a buyer will want to check that required filings have been made and records are up to date.
* Depending on the transaction, the buyer’s advisers may want to look at previous board or shareholder resolutions to ensure that key historic transactions have been validly entered into.
* A buyer would also want to know if there is a pattern of smaller issues. For example, repeated late or poor filings which may indicate wider issues with governance or administrative processes.

**Past Acquisitions and disposals**

In relation to any acquisitions or disposals, the buyer would want to check whether the target has any ongoing obligations or liabilities under contracts pursuant to which it acquired or disposed of subsidiary companies and/or businesses. Typical examples of points to look out for are:

* outstanding warranty or indemnity periods (including for tax);
* non-compete and other restrictive covenants;
* any conditions still to be satisfied;
* other “live” obligations such as deferred or additional consideration;
* confidentiality obligations; and
* any post-closing undertakings (e.g. to provide services/products or support after completion) which are still live.

In the event that the target or any subsidiary is not a wholly owned subsidiary, the buyer will want to investigate the shareholder dynamics and rights including the terms of any shareholders’ agreement.

**Separation Issues**

The buyer will need to investigate the relationship between the target group/business and the seller’s group. It will also want to ensure that the assets subject to the transaction sit in the right place at completion such that the target group/business can cleanly detach from the seller’s group. Examples of key points to look out for include:

* Assets that are not owned by the target group;
* Contractual relationships or operational dependence on the seller’s group. If the target group/business is reliant on services or supplies provided by the seller’s group, for example, the buyer will need to consider if it can replicate or replace these post completion; and
* Guarantees given by the target group in respect of seller group obligations.

**Insolvency Searches**

A buyer would want to ensure that neither the target company nor any seller is subject to any kind of insolvency proceedings. Necessary searches would therefore need to be carried out to ensure that the seller, in the case of an individual has not been declared bankrupt and, in the case of a company has not been put into administration, for example or that there are no pending petitions. Obviously, a buyer does not want to acquire a target that is in this position, but neither would it want to transact with a seller in this situation. In some cases, a transaction entered into with such a seller could be considered void.

**Regulatory/General Compliance**

A buyer will want to ensure that the target or seller has adequate policies and procedures in place to ensure compliance with their regulatory obligations. Key areas include data protection, anti-bribery and corruption and modern slavery.

**Material contacts, e.g. supplier contracts, customer contracts**

There will be a number of key issues that a buyer’s advisers will look for in their review of material contracts. Examples include:

* Are there any contractual restrictions on transfer, for example, change of control provisions (in the case of a share sale) or assignment provisions (in the case of an asset sale).
* Under what circumstances are the parties entitled to terminate the contract?
* When are the contracts due to expire and does any party have renewal rights?
* Are there any negotiations in relation to those contracts that are currently in progress?
* Are there any particularly unusual or onerous terms?
* What are the payment obligations under the contract, are there penalties for late payment or any price review provisions?
* Are there any non-compete/exclusive dealing obligations?
* Have key contracts been documented/properly documented and executed and what is the governing law?

The input of a commercial lawyer may be required in relation to any material contracts that are identified.

**Material Litigation**

The buyer will want to know whether the target is affected by any material existing or threatened litigation and if so the relevant details, the most obvious being details of the litigation itself along with the amounts involved. This is particularly important on a share sale.

The input of a litigation lawyer may be required in relation to any material litigation that is identified.

**Summary**

* Legal Due diligence covers a number of key areas including general corporate areas as well as more specialist areas.
* Corporate due diligence can cover a wide range of areas in relation to the company, the shares, past transactions, contracts and general compliance.
* The level of due diligence and the areas included in the due diligence will depend on a number of factors such as:
  + The buyer’s approach to risk;
  + The deal structure; and
  + The type of company, business or assets being acquired.