

Due Diligence

Seminar on Private
Equity – Challenges
and Opportunities

WIRC-ICAI-9.8.2014
@ Mumbai



Due Diligence (DD) – Definition

*Valuation is the process of determining the “Economic Worth” of an Asset or Company under Certain assumptions and limiting conditions and subject to the data available on the valuation date.

** Source -International Valuation Standard Council*

Due diligence is the framework to validate the “ Economic worth ” and subject to the data

“DD is Data Driven Drill Down (DD)”

Types of Due Diligence

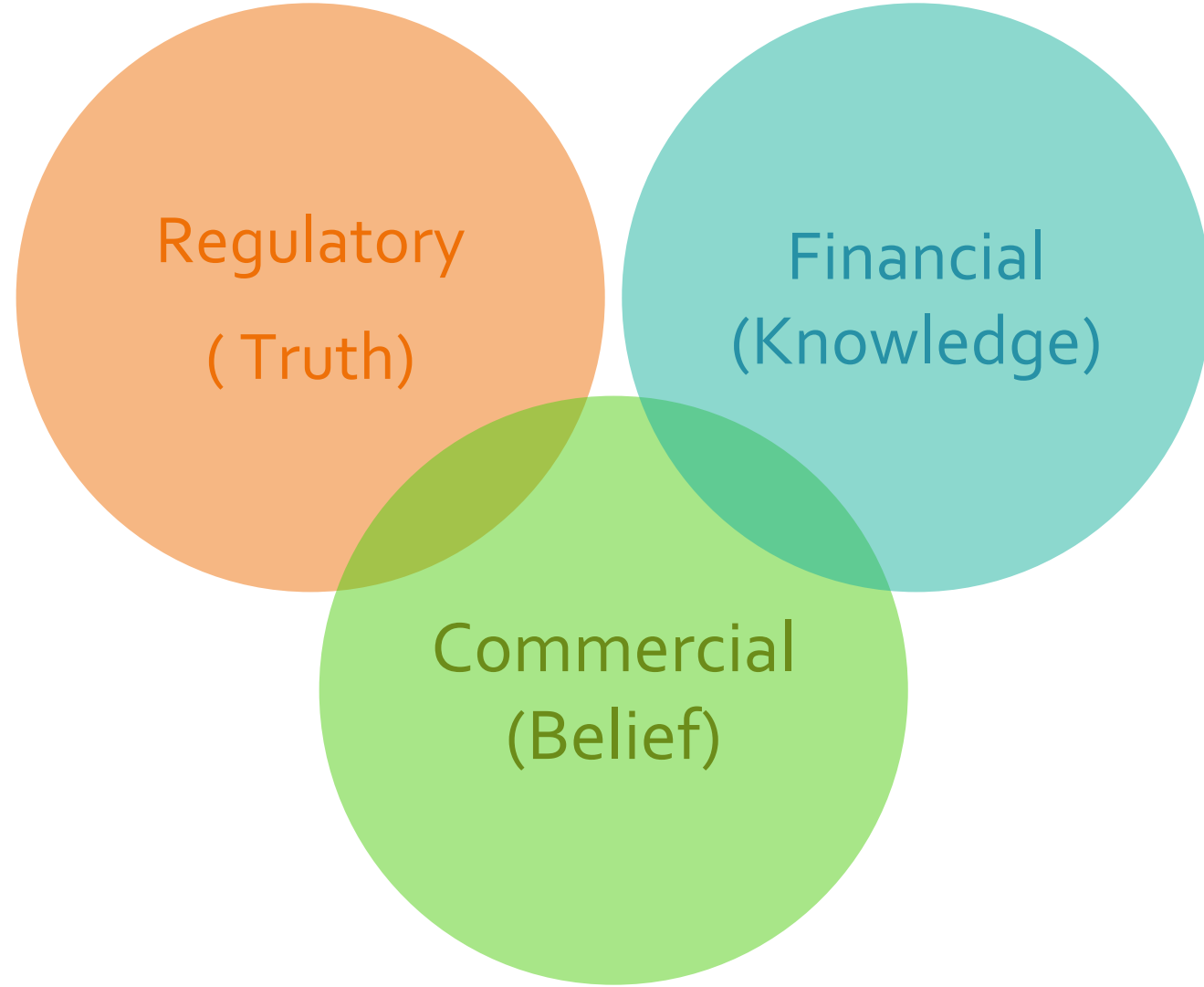
Not an investigation nor an audit

- Regulatory legal compliance (Non-Tax compliance)
- Financial & Tax compliance
- Commercial
- Technical (Intangible or Tangible IP/Process etc)
- HR (Emerging people centric Services business)
- Forensic (Recent trend in India – Post funding)

Overlap in Due Diligence domains

Some information requested & areas of focus may be repeated in different diligence conducted by different teams/agencies.

Advise to have cross functional engagement/debriefs across teams during DD



DD - Regulatory Compliance(& HR)

Process : Check-list driven

Follow-on :

Insertion of conditions precedents as part of SHA/SSA docs

-  Incorporation of company, MOA, AOA. (Including overseas entities, if any)
-  Company structure (Holding-Sub, shareholding & cap-table
-  Org chart & devolution of authority from BOD
-  MCA, Oher statutory filings – India, Overseas filing etc
-  Labour law, Exchange controls Returns/Billing data (e.g.STPi, Ex-Im) and country specific controls
-  PIPE deals – Listing and corporate governance structure
-  IP rights (Patents, TM's, Copyrights etc.)
-  Contracts with promoters, key management employees
-  Contracts with outsourced services providers
-  Details of any pending lawsuits, penal proceedings against company (Non-Tax laws – State/Central/Local/International)

#indicative list, not exhaustive

DD - Financial & Tax

Process : Focus on score keeping & number crunching

Follow on :
Term sheet numbers
realignment (Net worth,
valuations built around
financial scenario)



Accounting Framework as per AS



Financial and Non-Financial IT platform to capture data



Assessment, Returns compliance under Direct & Indirect Tax



Org chart & devolution of authority from BOD



Last 3/5 years audited statements, disclosure



Company's budget & business plans



Company's MIS reports, reconciliations



Schedules of AR (Customer segmentations), AP,
Inventories/Projects



Company's Fixed Asset – Tangible, Intangibles (e.g.
Cloud/SAAS)



Transfer Pricing, Related Party Transactions and Internal
audit



Bankers /NBFC info filing, limits and Grants (Solar energy)

#indicative list, not exhaustive

Commercial DD

Business Speak – Integrate well

Follow-on :

Revenue & cost – All
is well ? - Black/White

Term Sheet/SHA/SSA



Competition/ Market intelligence , company's standing in market



Org chart & devolution of authority from BOD



Clients/Vendors contracts, KYC & records updation



Channel structure for Sales, list of partners, intermediaries & their contracts



Nature of customers/vendors engagement –
One time, recurring (ageing of relationship) and financial impact



NDA's , Master Service Agreements, Joint
Venture Deeds, Royalty & revenue sharing, cost apportionments



Government related contracts – India and International



Overhead s like leave.license, staff facilty,
communication, capex

#indicative list, not exhaustive

Investee Company
Should make
business PE/VC
ready well in
advance to mitigate
risk during DD



LEGAL

- Diagnostics of legal & statutory records & compliances
- Ensure & facilitate a proper indexed arrangement of all legal regulatory compliance
- Setting up of Virtual Data Rooms and periodical updates in specific folders set-up goes long way in managing process



FINANCIAL

- Diagnostics of finance, data validation to ensure integrity of financial statement
- Tracker on yearwise tax data in structured manner
- Creation of requisite MIS, reports & dashboards for Due diligence team



COMMERCIAL

- Accumulation and presentation of client, vendor data
- Facilitate & ensure standard KYC & master revenue/procurement agreements
- Industry analysis & business practices for market, channels, customers segmentations

Law of the land

CFO should
have an Eagle's
eye-view

Cross
functional
preparedness

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