

# An Investor's Guide to Legal Due Diligence of a High-Tech Company

Written  
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## 1. Introduction

When an investor decides to invest in a company there is usually an exhaustive research process called a due diligence that an investor would undertake before proceeding. It is an information gathering process carried out by a professional adviser whereby an investor would determine all possible information about the business/assets including (i) whether to invest in the business (ii) if so, on what terms; (iii) at what valuation (iv) the validity of the information provided including past performance and the credentials of the directors; and (v) the potential represented by the business plan. The purpose of a due diligence therefore is to enable an investor to decide whether to proceed with an investment, establish areas of risk that may require particular attention and to observe how the company is addressing such risks i.e. the risk management measures the company has in place and ultimately

whether it would be worthwhile investing in this business or whether to withdraw.

In undertaking a legal due diligence an investor's advisor would request legal documents and in some cases interview board members, managers and staff. However, there are other types of due diligence that an investor may carry out such as a financial, commercial, technical and management due diligence. In this guide, Dr Rosanna Cooper of RT coopers will focus on an investor conducting a legal due diligence.

The target company should be prepared for its documents to be scrutinised by professional lawyers. Investors usually concentrate on two types of due diligence, business and legal. Dr Cooper provides a checklist for investors intending to undertake a legal due diligence, however, this list is by no means an exhaustive one.

## 2. Legal Due Diligence

RT Coopers conducts legal due diligence of companies. When we are instructed to carry out a legal due diligence, the firm sends a due diligence questionnaire to the target company requesting detailed information from the company and to reply to the questions within a limited timeframe, to keep in line with the investor's timescale. From the information received, the firm would compile a report and make key recommendations to the investor. See the key aspects of a due diligence checklist outlined below. An investor would generally expect a company to hand over the following key documents such as:

- Employment contracts
- Board minutes, resolutions and any minutes of shareholders meetings
- Signed confidentiality agreements
- Licensing agreements and assignments including any agreements with employees
- Articles of Association and Memorandum of Association
- Terms of Business
- Any litigation-related documents
- Any patents, copyrights, trade marks and other intellectual property-related documents

### 3. Due Diligence Checklist

Below is a checklist of the key aspects of a legal due diligence:

#### □ Corporate Documents

- A list of all corporate documents including organisation chart, subsidiaries and other affiliates, percentage ownership and jurisdiction of each subsidiary
- A list of directors and key management/supervisory staff
- Summary of number of employees
- Stock transfer and certificate books, ledgers and records of the company, class of shares and list of shareholders
- For each class of debt, provide listing of debt holders
- Names, addresses, and contacts of company's professional advisers
- List of major clients and their locations

#### □ Securities

- Shareholders agreements
- All stock option, stock purchase and other employee benefit plans and forms of agreements
- Any private/public commitments relating to the stock of the company
- Any debt arrangements, guarantees or indemnities between the directors and shareholders

#### □ Litigation

- Copies of any pending or threatened litigation, arbitration, claims and proceedings involving the company or the founders
- Summary of disputes with suppliers, competitors, or customers
- Correspondence with auditor or accountant regarding threatened or pending litigation, assessment or claims.
- Orders or judgments of courts or governmental agencies
- Settlement documentation

#### □ Employees and Related Parties

- Summary of any threatened or pending employment disputes
- All employment and consulting agreements, loan agreements and documents relating to other transactions with officers, directors, key employees and related parties
- Schedule of all compensation paid to officers, directors and key employees for most recent fiscal year
- Summary of employee benefits and copies of any pension, profit sharing, deferred compensation and retirement plans
- Summary of management incentive or bonus plans not included in (7) above, as well as other non-cash forms of compensation.
- Confidentiality agreements with employees

#### □ Financial Information

- Audited financial statements since inception (unaudited if audited financials are unavailable).
- Copy of business plan
- Revenue, gross margin and average selling price by product or service

- Copies of any valuations of the company's stock
  - Description of all contingent liabilities
- **Property**
- List of real and material personal property owned by the company and all accompanying documents
  - All outstanding leases with an original term greater than one year for real and personal property to which the company is either a lessor or lessee.
  - Documents pertaining to proprietary technology developed/owned by the Company, including any copyright or patent filings. This will also include information confirming that the Company's systems, software and technology is owned solely by the company and does not infringe on any other party's rights.
- **Taxation**
- Any notice of assessment and income tax returns for the last three years
  - Evidence of company being current on all tax liabilities
- **Insurance and Liability**
- Schedule or copies of all material insurance policies of the company in force
  - property, liabilities and operations, including product liabilities
  - Details of any assets pledged as collateral
  - Details of the company's compliance with loan covenants
  - Details of all financial liabilities, recorded or contingent of the company
  - All other relevant documents pertaining to the company's insurance and liability exposure
- **Acquisition, Partnership or Joint Venture Agreements**
- All acquisition, partnership or joint venture agreements.
  - Documents pertaining to potential acquisitions or alliances.
  - Any agreements regarding divestiture of assets.
- **Governmental Regulations**
- Summary of health and safety enquiries for past three years
  - List of any governmental licences and or regulations and compliance
- **Intellectual Property**
- List and copies of patents held and applications made by the company
  - List of trade marks, copyright and design held and applications made by the company
  - Identify all persons who created or participated in the creation of the company's intellectual property
  - List and copy of licenses for any form of intellectual property held by or granted by the company
  - Description of any pending or threatened infringement claims by or against the company
  - Description of any important know how owned or licensed to the company.
- **Products and Equipment**
- Copies of all material agreements/documents, list and copy of all contracts with dealers, distributors, agents and others

- Copies of product(s) warranties of the company
- All equipment leases

□ **Environmental Matters**

- List and description of all current environmental litigation or proceedings
- Copies of policy memoranda, programs, procedures, training courses, emergency plans etc. relating to the environment
- List of all environmental permits and licenses required for the company's' activities
- Description of the production and storage and related environmental risks
- Description of any emissions into air or water; waste water and other discharges; noise pollution and waste produced
- Description of any enquiries, inspections, examinations, investigations by environmental authorities
- Description of any injuries or illnesses of personnel, accidents, during the last five years, with effect upon environmental matters.
- Description of any other relevant matters with respect to the environment.

#### **4. Conclusion**

RT Coopers are specialists in corporate finance and regularly undertake due diligence work on behalf of our investor clients.

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