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THE TRUE OBJECTIVE OF DUE DILIGENCE

By Anna Gorkun, Associate

The initial response to the question "Do you have an interest in acquiring "ABC" company?" would be "Tell me about it" rather than "What is the price?" Due diligence, in general, is an investigation of the business in connection with a (possible) transaction. Its main objective is to accumulate sufficient information for business decisions to be made by the client. There is much to be learned about a particular business. As most businesses are purchased because of the upside they might bring to a buyer, what really matters is their potential, which is often measured by their history. It goes without saying that what is important to a buyer varies from a deal to a deal and from a buyer to a buyer. The task of the professional due diligence expert is to understand the client's needs and readily identify problems and risks pertaining to a particular business.

One may consider due diligence as ultimately an exercise in risk allocation, in the context of negotiation of terms, price adjustment, or indemnification. A seller and a buyer must each assess the risks they are ready to take. Superior knowledge about the target is the key to having a favorable position to negotiate with the other side. A party with superior knowledge will achieve a negotiating advantage, because of its ability to value each risk, estimate the perceived costs for risks, bargain for more favorable terms, and even shift to the other party the most costly risks.

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