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WHAT TO EXPECT FROM LEGAL DUE DILIGENCE

Business competitiveness among rivals in similar industries is fierce and demanding. The current trend of business expansion is for stronger and financially healthier corporations to merge, acquire, and take over other corporations. Over the past few years, we have heard merger and acquisition (M&A) news or proposals on a daily basis. However, we do not hear as much about the details that make an M&A successful, especially when it comes to due diligence.

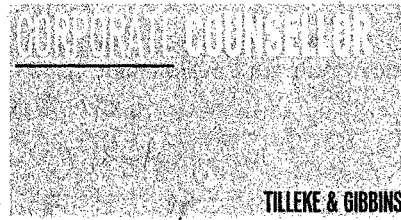
Most businesspeople are familiar with the general concept of due diligence, but many have questions about precisely what it entails and why it is vitally important. Legal due diligence has a variety of definitions, depending on the context. Generally, due diligence refers to the conduct and judgement that a person would take to carry out their duties. In a corporate context, due diligence is more of an analytical and investigative exercise, typically involving the feasibility of a major transaction.

Before any merger or acquisition is completed, financial due diligence on the target is required for the acquirer to decide whether the acquisition is commercially and financially viable. Legal due diligence is also important to identify any legal discrepancies or liability on various matters.

For the acquirer to carry out the due diligence, sincere cooperation from the target is needed, as many documents are not publicly available. The acquirer must therefore rely on the target to submit documents in line with a checklist provided by the acquirer or its legal team. The legal team will attempt to confirm many legal issues, including: the legitimacy of the issued shares to be sold to the acquirer; whether the target is legally authorised to conduct the business with the proper or required licences; whether the shares or businesses to be sold exist validly with a legitimate structure; terms and obligations of material commercial contracts and employment agreements with key management personnel; and, most importantly, whether or not there is any

pending litigation filed by or against the target and/or its management, or even a bankruptcy or reorganisation filing.

From our experience, depending on the size of the target and the value of the deal, due diligence can take seven to 30 days to complete. Supporting documentation for each fact would be attached to the report. This information will be reviewed by the acquirer's management team, which may then wish to consider possible adjustments of the sale price, provisions on representations and warranties by the target or responsible management, amendments of any discrepancies before the M&A concludes, and continuation or minimum employment period of the key employees.



Due diligence materials can be annexed as schedules to the main report for disclosure by the target and can be used to obtain approval of the deal from the board of directors and/or shareholders of both parties.

Apart from the above, other determining factors can be uncovered through the legal due diligence process that may eventually make or break the deal. Examples include noncompliance and violation of laws and regulations, restrictions on foreign ownership, restrictions on share transfers, encumbrances on major assets, change of control provisions or any provisions that would restrict the contemplated acquisition contained in contracts entered into by the target; breach or potential breach of contract or termination or potential termination of material contract, and so on.

Although these findings must be carefully considered by the acquirer's management, it is important to recognise

that there are certain limitations when performing legal due diligence review.

First, Thailand does not have a centralised recording system of pending nationwide court suits to arrange for litigation searches. Generally, jurisdiction over the case rests with the court located at the place of domicile of the defendant or the place where the debt occurred.

Independent litigation searches have to be conducted at each major court in Bangkok—the Central Bankruptcy Court and the Business Reorganisation Office, Civil Court, South Bangkok Civil Court, Intellectual Property and International Trade Court, Central Labour Court, Criminal Court, and Central Tax Court. If the target is located outside Bangkok, litigation searches at that provincial court also must be arranged.

Another limitation is that Thailand lacks a centralised asset registry. Real property searches have to be arranged at the relevant Land Office where the target's real property is situated. Copies of the land title deeds would, however, serve to facilitate the conduct of these property searches.

Finally, any encumbrances on shares can only be verified by vetting the Register of Shareholders, which is maintained solely by the target and is not in publicly available records.

Despite these limitations, due diligence can reveal crucial information. Although there are no specific statutory requirements in Thailand for legal due diligence to be conducted during the course of an M&A deal, due diligence reviews are now widely seen as an essential step. All companies involved in significant transactions should carry out legal due diligence review, whether limited or in full, prior to entering into any M&A deal in order to prevent or mitigate future liability.

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