

ACQUISITION AND DUE DILIGENCE IN SWEDEN

DELPHI & Co, Anders Strid

BACKGROUND

Up until rather recently (about 10-15 years ago) the concept of due diligence investigations was not widely spread in Sweden, even among lawyers. The normal procedure for a buyer of the stock of a company or its business was not to conduct a due diligence. The buyer did normally rely solely on the warranties and representations given by the seller and to hold some of the purchase price in escrow for a period of time. As time elapsed, transactions became more complex and internationalised and foreign buyers companies wanted to conduct due diligence investigations on the target companies. This led to a gradual change in the whole purchases process in which the due diligence investigation nowadays forms an integral part.

The Swedish Sales of Goods Act applies when buying shares or the business of a company. The general view is that a buyer is not obligated to investigate the company that he contemplates on buying. However, if asked by the seller to investigate the company, he is put under an obligation to investigate the company. If the buyer chooses not to investigate the company, he will not be able to claim compensation for faults relating to the company that he would have been able to notice during a due diligence investigation. However, if the fault falls under a warranty given by the seller, the buyer will still be able to claim compensation for breach of warranties. Naturally, there are qualifications as to what has been stated above. Depending on the circumstances the seller may be under an obligation to inform the buyer on certain issues in relation to the company.

HOW TO CONDUCT AN ACQUISITION

This section sets out the most common bits and pieces in a private/negotiated transaction when acting for the buyer. I have chosen not to elaborate on issues associated with public and limited auctions as well as public offers.

The initial contact between the seller and buyer is normally undertaken without the involvement of lawyers. During this stage the main commercial terms such as the price is being decided. Thereafter, the lawyers are brought into the playing field. A time schedule for the transaction should then be decided. Such a time schedule sets, *inter alia*, out the time frame for the due diligence investigation together with the signing and closing date. The time schedule should be kept as tight as possible not to allow the acquisition process to lose momentum.

Thereafter a Letter of Intent/Heads of Agreement/Memorandum of Understanding setting out the general framework of the transaction is to be negotiated and signed by the parties. An important part of this document is the form and volume of the due diligence investigation and how the due diligence will effect the seller's liability for breach of warranties under the purchase contract. It is also of importance to state as to how binding the Letter of Intent is on the parties and to regulate the confidentiality of the contemplated transaction as well as the buyers exclusivity to negotiate with the seller for a limited period of time.

In order to gain time and to help keep the transaction confidential, it is advisable to conduct the due diligence investigation and contract negotiations simultaneously. Once the due diligence investigation is over and the purchase contract has been negotiated, the time has come to sign the contract and close the deal.

If there are any conditions that has to be fulfilled before closing can take place, such as for example clearance from relevant competition authorities, signing and closing has to take place on different occasions.

As soon as practically after closing has occurred an extra shareholder's meeting should be held at which the former members of the board of directors are being discharged and a new board of directors of the company should be elected.

The former board of directors should issue a Power of Attorney vesting the new board of directors power to act on behalf on the company until the new board of directors has been formally registered with the Patent- and Registration Office.

The transaction has now been finished and the only thing that remains is to follow up on warranties given by the seller and if the conditions have been fulfilled according to the terms of the agreement, if applicable, release the part of the purchase price that is being held in escrow.

HOW TO CONDUCT A DUE DILIGENCE INVESTIGATION

This section deals with the more or less standardised parts of a due diligence investigation. Of course a due diligence investigation varies from case to case depending on the size of the transaction contemplated and the operations of the target company.

Several different advisers, depending on what is to be investigated, normally take part in a due diligence investigation. Auditors and tax consultants normally see to financial and tax matters, whereas lawyers investigate sees to the rest. Sometimes, depending on the business of the target company, it is advisable to bring in technicians that are experts on technical aspects of environmental issues.

Delphi & Co has a solid reputation when it comes to environmental law and has an extensive network of technical consultants that we work closely with during due diligence assignments.

Depending on the size of the transaction, the time available, and the wishes of the buyer, an in dept or a limited investigation is performed.

The first phase of the process is to have the client to sign an engagement/client letter setting out, among other things, the extensity of the investigation and the liability of the law firm in relation to the assignment.

The second phase is to provide the seller with an enquiry list in relation to the target company. Before the actual investigation commences it is standard procedure to search public registers for useful information (se below) regarding the target company.

The buyer and his advisors will, normally, enter into a confidentiality agreement provided by the seller before gaining access to any confidential corporate documents. In general there are restrictions as to reproduction, use of scanner, dictaphones, cameras etc in the data room containing the documents provided by the seller.

Sometimes the buyer is given the opportunity to interview management and/or members of the board. This is an opportunity that shall not be pass on. For this purpose a question list is often prepared.

Once the actual fact finding phase is over a due diligence report is written. Such report is normally divided into different sections. The first section sets out issues in relation to liability, limitations on the investigations and assumptions made by the investigators. The next part is the Executive Summary in which significant findings are highlighted. Thereafter the report breaks down in standard sections such as Corporate, Intellectual Property, Employees, Properties, Environmental etc.

Depending on the findings made during the investigation additional questions may have to be forwarded to the target company as well as the demand for more documentation.

ACCESS TO PUBLIC RECORDS

Corporate

- Memorandum of Incorporation.
- Certificate of Registration. The certificate contains information on; inter alia, the share capital of the company, number of shares, the members of the board, the auditor/s, fiscal year of the company etc.
- Articles of association.
- Minutes of ordinary and extra annual meetings with the shareholders' of the company.

All the above documents are available at the Patent- and Registration Office. Delphi & Co can access certificates of Registration on-line.

Financial

- Audited annual reports. Audited annual reports can be obtained from the Patent - and Registration Office.

Tax

- Tax assessment forms. These can be obtained from the Tax Authority.

Real Estate

- Excerpt from the Land Registry regarding real estate owned by the company. Said excerpt contains, inter alia, information regarding the owner of the property, registered encumbrances of the property, and if the property has been mortgaged. However, it is not possible to see if the mortgages have been pledged as security.

Delphi & Co can obtain excerpts from the Land Registry on-line.

Floating Charges

- Excerpt from the Registry of Charges. This excerpt contains information on floating charges taken on the business of the company. It is, however, not possible from the excerpt to see if the floating charges have been pledged as security.

Intellectual Property Rights

- Excerpts from the Patent- and Registration Office regarding patents and trademarks held by the company.

Environmental

- Copies of the company's annual environmental reports (if applicable).

All companies that conduct environmental hazardous activities, which needs a permit to do so must submit an annual environmental report to the local County Administration Office. The report must contain information on all environmentally related permits held by or applied for by the company. Using the information in the report it is possible to obtain copies of the permits from the respective authorities that have granted them. However, gaining such information is much more time consuming than obtaining any of the other above-mentioned company related documents

The above mentioned information is rather easily obtained and you will have it in a day or two, apart from environmental permits.

It is of course possible to obtain more publicly available information in relation to the target company before conducting a Due Diligence. However, that may prove rather time consuming and is therefore often not worth the time and effort. Such information is normally asked for in the enquiry list submitted to the target company, or obtained during interviews with the management or the board of directors.

I hope that the brief information contained in this memorandum is suffice and will be of help to you. Should you have any questions, please do not hesitate to contact me.

Yours sincerely
DELPHI & Co
Anders Strid and Johan Bogren