



EBAN

DUE DILIGENCE GUIDEBOOK FOR ANGEL INVESTORS

2024



1. SUMMARY

Key findings of Due Diligence Exercise

The aim of this document is to provide a template for a due diligence report, and some ideas for questions to ask and lines of enquiry to make. The list of questions is not intended to be comprehensive, and many may be inapplicable to certain companies. Clearly with a wide range of business models, stages of development and trading history, this will never be a “checklist” exercise. The template is therefore intended as a guide as to the principal areas to cover and a starting point of questions to ask. Depending on the answers, some areas will certainly need more thorough investigation. A further aim is that we have some consistency in the due diligence exercise, to allow the investment committee to compare different investments.

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2. CORPORATE STRUCTURE AND OWNERSHIP

Objectives: Identify if there are any issues with the ownership structure that may cause us difficulties/conflicts of interest in the future, or be prejudicial to our shareholder interest.

- What Corporate Structure is used
 - Who are the shareholders
 - List by shareholding
 - Identify who are
 - Full time active in the company
 - Non full-time but active investors
 - Passive Shareholders
 - Corporate Shareholders
 - Identify shareholder objectives for all major shareholders
 - If Corporate shareholders exist, what is objective of shareholding
 - Depending on split may be necessary to speak with all principal shareholders.
 - Identify any possible conflicts or difficulties with different shareholder interests.
 - Are there any subsidiaries
 - If these exist, how are they managed.
 - Documents to be provided.
1. Articles of Association and Memorandum, together with a copy of the company's latest annual return to Company's House. Copies of all shareholder agreements still in force
 2. Current share register and details of different classes and rights, if applicable
 3. Copies of all shareholder agreements still in force
 4. List of proposed new investors with likely amounts to be invested and any conditions applicable.
 5. Details of all outstanding share options, warrants, conversion rights or other agreements that may result in further shares being issued.
 6. List of any subsidiaries with percentage owned, purpose of company, name of director(s), and latest sales turnover, net profit and balance sheet.

3. FINANCIAL

Objective: Ensure we have a true and accurate picture of the financial state of the company, and realistic projections going forward

- Examine the accounts that exist. Are there any previously documented business plans with which to compare them? If not, why not?
- What are the key revenue items for the business? How reliable are they going forward?
- What are the key costs of the business? How are these likely to evolve over the next 3 years. How might they be reduced if circumstances required it?
- What are the assets on the balance sheet? If there are any unusual items, how is the value arrived at?
- What intellectual property assets does the company own, including registered rights (e.g. trade marks, designs, patents, utility models, plan variety rights) and other protection measures (e.g. copyright, trade secrets, domain names, databases)?
- What is the value of the company's intellectual property? Is the company achieving financial gain through it?[1]
- Has the company signed any intellectual property-related licensing agreements, either as a licensor or a licensee?
- Does the geographical scope of the company's registered intellectual property rights match the business and internationalisation strategy of the company (e.g. does it own an EU trade mark if selling or planning to sell throughout the EU or a registered trade mark in a relevant country beyond the EU)?
- Look at the debtors register. Is this company having difficulty getting paid. If so, why? Has the company filed all necessary tax returns (TVA/VAT, Profit related Tax etc).
- Is the company benefiting from any government grants/loans etc and if so on what terms
- Required Documents

7. Copies of the last three audited (or provisional) annual accounts.

8. Sales and estimated net profits during the current financial year to date and an estimated balance sheet at the latest available date. Details of any material changes since such balance sheet.

9. Details of any loans, overdrafts or other indebtedness currently outstanding.

[1] For a quick and easy way to analyse a company's intellectual property to determine how it may impact its business, check out the free IP Scan online tool on the Ideas Powered for business website (<https://business.ideaspowered.eu/>). EBAN is a member of the Ideas Powered for business network, managed by the European Union Intellectual Property Office (EUIPO).

10. Documentation relating to any government grant/aid or loans.
11. Projections for the current full financial year and four further years, including sales turnover, gross margin, overhead costs, EBITDA, net cash flow and year end cash balance.
12. Contact details of the company's accountants and authority for us to speak to them about the company's financial affairs.
13. Name and contact details of the company's principle bank and authority for us to contact them to obtain a standard bank reference.
14. Details of any current or anticipated legal action or tax enquiries affecting the company. Name of legal adviser and permission to speak to them if any legal action pending
15. List of premises occupied, leased or owned by the company with rents payable and dates of lease expiry or break clauses.
16. Summary of principle insurance policies.
17. Intellectual property portfolio (e.g. registrations, applications).
18. Intellectual property valuation report/s[2].

[2] There are qualitative and quantitative approaches to intellectual property valuation. With regards to the quantitative valuation, three methods are used in accordance with international standards for intellectual property valuation: the cost-, the market-, and income-based approaches.

4. BUSINESS PLAN

Objective: To ensure that the business plan is realistic, based on reasonable assumptions and that the ideas behind it have been tested.

- What are the key assumptions behind the business plan? What evidence exists to support these assumptions?
- What will be the key challenges in achieving the business plan?
- What are the USPs of the business? What is the evidence that they are genuinely unique? How sensitive is the business plan to changes in the price and volume of sales?
- How sensitive is the business plan to sales developing more slowly than planned? What is the planned use of funds? Is there a detailed and realistic budget for this?
- Are the costings complete – e.g. are there allowances for extra overheads etc as the business grows? Are there any other “holes” in the budget?
- What is the competitive position of the business? How are the claims with respect to the competitive position justified?
- Who are the main competitors? What are their strengths and weaknesses? Has an analysis been conducted of the competitors’ intellectual property portfolios and any potential related threats and opportunities?
- If this is a novel product or service, what evidence exists that there is a demand for it? Has any trial, market research, freedom to operate, feasibility study, etc. been carried out? Are the innovative products or services protected by any intellectual property rights, or does the company plan to protect them?
- Does the company have an intellectual property strategy, including an intellectual property commercialisation plan? If so, how is it aligned with its overall business strategy and goals?
- What are the main dependencies on third parties? Do they look reasonable? What are the barriers to entry for competitors if the idea is a success?

5. SALES AND MARKETING

Objective: To be confident the company has a plan and the skills to get their product or service into the market and sell it profitably

- What is the go-to-market strategy for the business. What makes them think it will work?
- If there is a significant marketing activity (and spend) planned for this business, what evidence is there that it is well focussed?
- What is the evolution of sales in the last three years?
- Who were the top ten customers in the last three years? Have they changed? Have any major customers stopped doing business with the company. If so why?
- Have there been any significant customer disputes in the last three years, whether taken to court/tribunal or not.
- Has the company had to issue any refunds/credit notes etc for any reason What is the sales projection for the next three years? What is this based on? What is the forward order book?
- What is the current sales pipeline? How are win % arrived at? What significant customer contracts currently exist?
- If the sales strategy involves third party channels, what arrangements are in place. What contracts/partnerships exist?
- What evidence is there that the pricing model is correct?
- Can they supply a high profile customer reference who would be happy to speak to us
- Has intellectual property protection been integrated into the company's branding strategy (e.g. has the company registered any trade marks or designs)?

6. ASSETS

Objective: to ensure the assets owned by the company have the value assumed in the business plan, and that such value will be protected.

- What technology or other important assets, including intangible assets, are owned by the business?
- Is it reliant on any technology provided by third parties to provide its product or service. If so what agreements are these covered under? Can they be cancelled?
- Is the technology patented, or in the process of being patented.
- If the business has developed a product or technology, what documentation exists concerning the product/technology e.g. product plans and roadmaps, specifications, design documentation etc. How easy is it to develop the technology further
- What is the current state of the development
- What Quality Assurance measures have been put in place to ensure the reliability of the product or service?
- How dependent is future development on key individuals?
- If funds are to develop a product, how have the development costs been estimated? What is our confidence level in these?
- Do employment contracts explicitly assign copyright to the company
- Have any of the company's products been developed outside the company i.e. by a third party organisation, or by non-employed independent contractors (even if working on the company's premises). If so, what measures are in place to ensure that the relevant intellectual property rights are owned by the company or that the company has taken the necessary steps to lawfully use and exploit these rights? For example, has a non-disclosure agreement (NDA) been signed between the company and the relevant third party or has a confidentiality agreement been signed between the company and its relevant employees?
- Are any Open Source items used in the company's products
- Details of any contractual obligations requiring payments to be made, eg royalties, license fees.
- List of all intellectual property rights owned or applied for and details of scope and protection and dates of expiry.

7. MANAGEMENT AND STAFF

Objective: Ensure that the company has the right people and is able to recruit and keep the necessary staff to execute its plan

- Who are the key people in the management team Identify skills and background, summarise career history Identify which are shareholders
- How will key non-shareholder management be retained/ incentivised?
- Are there any significant gaps in the expertise of the management team, looking forward as the company grows?
- What recruitment is needed over the next few years? Are there any problems anticipated with finding and keeping the necessary staff?
- Have there ever been any significant disputes with staff, whether taken to formal proceedings or not?
- Who owns the intellectual property relevant for the company, e.g. the founder/owner of the company, an employee of the company, a third party? For example, is the company's intellectual property protected in case a relevant person leaves the company?
- Who is managing the intellectual property of the company (e.g. a dedicated unit, an in-house expert, or an external counsel)? Is there a policy in place for staff relating to intellectual property? If so, is the staff aware of this policy?
- How many staff have left over the last 3 years? Estimate staff turnover
- Are there any profit-share or other performance related schemes in place, and what are the potential costs.
- Documents to be provided:
 - List of all employees with job title, salary, and details of any unusual contractual terms.
 - Details of any union agreements if any.
 - Copy of standard employment agreement(s) used for the different staff categories.

8. OPERATIONS

Objective: Understand how the business is run and controlled, and whether this is “fit for purpose” both now, and under the growth planned for the next few years

- How is the company run? What responsibilities have been defined?
- Are the powers of the Managing Director formally defined?
- Are the power and authority of other Directors or senior managers defined (e.g. spending powers, authority to sign contracts etc).
- Is there a staff handbook or similar document
- What other documents exist defining company processes? What records exist of what decisions have been taken and why
- What management/board meetings take place, and on what frequency? What records exist of these?
- If the company plans to grow significantly, is there a plan to cope with all the implications of this e.g. premises, Infrastructure, new roles in the company etc.
- To what extent does the company rely on suppliers to be able to offer its product or service? What are the contractual arrangements in place? What is the supplier management approach?
- How sensitive is the business to changes in the price of supply

9. INTELLECTUAL PROPERTY CHECKLIST

This checklist was made possible thanks to our partners at the [European Union Intellectual Property Office \(EUIPO\)](https://www.euiipo.eu).

List of the registered intellectual property rights the company owns or has applied for, such as:

- national or EU trade marks,
- national registered designs or registered Community designs (EU level),
- breeder rights / plant variety rights,
- patents,
- utility models.

List of other IP protection measures the company owns, such as:

- copyright,
- unregistered design rights,
- trade secrets,
- database rights,
- domain names,
- trade names,
- service marks.
- Claims of infringement or misappropriation of others' patents, copyrights, trade secrets, or other proprietary rights
- Copies of all agreements in-licensing or acquiring any technology, including without limitation software licenses, patent licenses, or other technology licenses, or any development or joint-development agreements
- Copies of all agreements out-licensing or selling any technology, including without limitation any software licenses, patent licenses, or other technology licenses, or any distribution, or sales-representative agreements
- Intellectual property strategy document
- Intellectual property-related NDAs and confidentiality agreements

10. LEGAL

Objective: To understand if there are any unusual legal obligations entered into by the business that may affect our view of its value

- Has the company signed any non-competition agreements (or agreements with such clauses in them) with any other party
- Has the company signed any exclusivity agreements (i.e. to not work with competitors of any of its customers) or agreements with such clauses in them
- What NDA's are currently in force
- Has the company ever been subject to legal proceedings, or the threat of them? If so provide details. Are any of them related to intellectual property infringements?
- Are there any other non-standard legal agreements the company has entered into, which may affect the value of the company?

11. RISKS

Objective: Identify the key risks that might prevent the business achieving the planned success, and any plans to mitigate them

- What are the key risks to the business in the view of the Entrepreneurs? What plans exist to mitigate these risks?
- Are there any further key risks identified by the Investigator, including intellectual property or intellectual property infringement-related risks (e.g. failure to implement measures to protect the company's intellectual property)?
- Does the company have an intellectual property enforcement strategy (e.g. a plan on how to address potential infringements or measures in place to not infringe others)?



12. OTHER OBSERVATIONS

Anything else of note uncovered.

13.RECOMMENDATIONS

- Further specific investigations required, (maybe by specialist in finance/technology/law etc)
- Further references/research required to resolve concerns.
- OK to proceed subject to certain conditions (e.g business employs specific skills)