DUE DILIGENCE

What are the trends and how to adapt?

Due diligence is an inherent part of the transaction process. It is difficult to imagine any investor willing to commit to an endeavor without having at least a basic legal, financial or business understanding of the situation he is planning to enter. At the same time, ever changing regulations, market trends and different objectives of transaction parties have direct and dynamic (!) impact on the way the due diligence process is structured. Analyses of targets in the US vary from those conducted in Europe or in Asia. Similarly, the type of transaction and entities involved will influence the way the investigation should be conducted.

The paper below aims to address some of these issues as it poses questions concerning the due diligence review with answers from experiences M&A practitioners from different parts of the world.

1. What are the trends you see in your jurisdiction with respect to the scope of the legal due diligence review? Do you see any specific difference in the scope of due diligence review depending on the transaction structure (share or asset deal), the transaction process (structured auction process and its phases or one-to-one deal), vendor or purchaser due diligence? How are the limitations of the scope dealt with in the SPA?

Bulgaria

Legal due diligence in any transaction is the key tool to mapping and assessing legal risks which might affect target valuation, deal structure and timing. There are no identical transactions and targets and there is no “one size fits all” due diligence review. The scope of legal due diligence review varies widely depending on various factors discussed below.

Full scope due diligence review is usually the client’s preference in most of the transactions and buy-side mandates. Without limitation to the scope of due diligence specific emphasis is often put on, and more profound investigation is carried out, with respect to particular areas of relevance to the specific industry where the target operates or with respect to sensitive areas of the target’s business itself.

At the same time we see a trend of limited scope focused purchaser due diligence review in some transactions especially in structured processes where reliance on the vendor due diligence report is provided to the bidders. In other instances client’s request for a limited scope purchaser due diligence is driven by the unsatisfactory quality of the available due diligence information provided by the seller, the client’s budget restriction, the timeline of the transaction and finally by the client’s appetite for risk.

In structured auction processes limited scope due diligence is usually carried out by the bidders during the initial phase of the process when potential buyers rely very much on the vendor due diligence report. Vendor due diligence report is usually full scope but only indicates some legal facts and issues without thorough assessment of the legal risks associated therewith. It is not uncommon that we are asked to do only a review of the vendor due diligence report and a limited review of some source documents and public registries in order to put together a high

profile bullet point list of key issues before indicative bid is made. Second phase due diligence in structured processes is more extensive in scope and usually covers all documents disclosed in the data room. Sometimes review of data room documents is subject to materiality thresholds and sampling agreed with the client as discussed below.

In one-to-one deals we see similarities in terms of buyer's approach to the scope of legal due diligence review. Limited due diligence review focused on specific legal issues and areas of concern is carried out by the potential buyer before indicative offer is made while full due diligence follows the signing of a term sheet.

On the sell side we often experience the willingness of the seller to limit the scope of the due diligence investigation amid fears for leakage of trade secrets and confidential information. In many cases when the potential buyer is a competitor, the seller does not feel sufficiently protected by the non-disclosure agreement and even by the restricted access to highly confidential information and potentially competitive sensitive information by a very limited group of buyers' advisors at an advanced stage of the transaction process.

Costs associated with conducting of the due diligence or responding to the due diligence questions by the seller are also a factor influencing the scope of the legal review especially in small scale domestic transactions.

In case of asset transactions we still see more detailed due diligence review because of the need to properly identify all assets subject to the transaction and assess their transferability as well as the assignability of each commercial contract included in the scope of the transactions and the potential transfer of undertaking implications on affected employees.

Limitations in the legal due diligence review and the disclosure process are taken into account in the SPA as follows:

- the definition of materiality used throughout the warranties reflects the materiality criteria applied in the course of the legal due diligence exercise;

- certain areas which are not reviewed thoroughly in the course of the legal due diligence because of lack of sufficient information are covered by warranties or by specific indemnity;

- sandbagging provisions are included in the SPA.

France

It should be noted that there are less asset deals than share deals in France. This is due to tax reasons, which make asset deals less interesting from a financial point of view. However, in case of asset deals, the scope of due diligence are reduced as it will usually not cover corporate and certain tax aspects. For the remaining, the scope remains the same and our review depends on which work streams the client wants us to highlight.

In one-to-one deals, scopes of due diligence may be narrower than in structured auction process. In the first case, clients sometimes review internally certain aspects of the business together with the legal aspects linked thereto in order to avoid having too much recourse to attorneys-at-law for due diligence exercises.

Vendor due diligences used to have wider scopes than purchaser due diligence. However, this tends to change these days as clients are putting pressure on fees, in such a way that even for vendor due diligences they accept to reduce the scope to the strict minimum, even carving out whole topics to fit in the budget they have allotted to due diligences, if need be.

Such limitations of scopes impact the drafting of the SPA, as warranties needs to be drafted in general terms in order to catch all potential situations of indemnification.

Poland

A noticeable technical trend in due diligence is the constant demand from clients to limit the number of requested documents and information concerning the target. This is linked with the increasing pressure to limit the duration and costs of the due diligence process, to maintain a high level of review or even to refrain from irritating the other party to the transaction. At the same time, of course, lawyers' must continue to secure the appropriate level of protection for their clients in transaction documents, tailoring it to the specifics of the deal and actual risks connected with it.

The need to limit the number of requests does not coincide with an ever-extending list of legal issues, which require verification by lawyers. More and more focus is required on cyber security issues, especially in light of a constantly increasing risk of hacks. The need to ask additional questions also arises from newly adopted laws. This includes both general EU regulations (such as the changes in data protection or the market abuse regulations) and more local solutions (e.g. last year's amendments to the provisions regulating transactions including entities owning land).

At the end of the day, the parties strive to ensure maximum protection in the transaction documents. The buyer wants full protection in the widest possible scope of representations and warranties, as well as indemnification clauses (is a specific risk is identified) and with the lowest possible limitations provided in termination and liability value provisions. The seller is usually reluctant to comply, especially in share deals in which the selling shareholders claim not to be fully aware of the details of the target's activities.

The Polish market still relies greatly on providing protection against sellers' representations and warranties in the transaction documents and transaction insurance is not widely practiced.

Due diligence is typically conducted by the buyer in order to assess the degree of risk associated with the planned acquisition and to determine the value of the assets, enterprise, organised part of an enterprise, or shares being acquired.

More and more often, it's the sellers who order a review of the target's affairs (a vendor's due diligence), to determine whether any unexpected irregularities exist that may disrupt the transaction's successful closing. A report from such review is then typically provided during due diligence to the buyer.

The subject of due diligence will vary depending on whether the transaction involves the sale of shares (a share deal) or assets (also depending on whether the assets will be sold individually or as an enterprise).

In the case of a share deal, analysis of the target's corporate documents is critical, and it is necessary to:

- First, confirm the existence of the shares and determine the rights attached to the shares

- Second, verify that the seller owns the shares and whether there are any encumbrances on the shares or restrictions on selling them.

Spain

Often times, tax matters are excluded from the scope of the legal due diligence entrusted to a law firm, since the review of tax matters is being handled by the same firm (audit firm, financial services firm, etc.) that is conducting the financial due diligence.

There might be differences in the scope of due diligence review depending on the following factors:

(i) Share *vs*. asset deal: there could be differences in the scope of due diligence in an asset deal if the purchaser does not intend to acquire all of the assets related to a particular business. Otherwise, the differences between due diligence in a share deal and an asset deal are not that many.

(ii) Auction process *vs*. one-to-one: in an auction process, the seller has more control over the due diligence process (scope, timing, etc.). In one-to-one deals, the purchaser may have more influence in how the due diligence process is carried out. In addition, an auction process is usually accompanied by a vendor's due diligence report, while these reports are not that frequent in one-to-one deals.

(iii) Vendor's *vs.* purchaser's due diligence: if the goal is to prepare a vendor's due diligence report that could be used by the purchaser there should be no differences between the scope of such report and the scope of a report prepared by the purchaser. If the vendor's due diligence report has limitations or excludes certain areas, the most likely scenario is that the purchaser will like to conduct due diligence over those areas.
From the law firm's standpoint, (a) in case the firm is acting for the seller, the scope of the report would be that of a full due diligence; and (b) if there is a vendor's report and the firm is representing the purchaser, then the scope of the due diligence will be confirmatory and there will also be a bring down due diligence.

Turning to the last question, the limitations of the scope of a due diligence review are usually dealt with through the representations and warranties included in the SPA.

USA

In the United States, the due diligence expectations among sophisticated parties in M&A transactions are fairly well-known. Due diligence is both exploratory and confirmatory in nature; in that the buyer is seeking to learn as much as possible about the business it intends to acquire and to confirm that what it has been told by the target's representatives is true.

The ultimate purposes of the due diligence process are:

- to obtain as complete an understanding of the target business as possible, prior to the consummation of the transaction;

- identify risks, underlying problems, legal concerns or business concerns that may exist;

- confirm the value of the target;

- provide relevant context to the drafting of transaction documents

- provide buyer an opportunity to assess whether its expectations regarding its target are correct and whether the transaction is appropriate and the transaction structure is optimal.

Since the nature of asset acquisitions is structurally more conducive to isolating liabilities than that of stock acquisitions, the scope of due diligence can be more circumscribed; for example, a buyer in an asset purchase transaction has more latitude in choosing not to focus on matters related to assets that not being acquired, liabilities that are being retained by the Seller, corporate ownership and history, and the like. Nevertheless, the more complete an assessment as is possible to obtain about a target, the more likely a buyer is to avoid surprises down the road. A buyer of securities, of course, takes on all problems and liabilities of the target unless they are separately carved out by agreement.

In auction sales, there is often a pre-arranged virtual due diligence data room prepared by the target's team and available for review. Whether the participants in the auction will have leverage to require substantially more information is highly dependent upon the individual situation, however, investment bankers leading the process for the target are usually quite experienced and provide the majority of what buyers will want to review. In highly competitive auctions, a bidder has the potential to gain an advantage over others by having its due diligence team engaged to perform the review early and quickly, in that a bidder who can provide a bid with a clearly defined transactional structure (and more certainty in advance as to changes, if any, it will require to the target's form of auction documents) has the opportunity to outflank bidders whose bids and structures are more heavily continent upon the results of their ongoing due diligence.

An important function of the legal team for the buyer's side will be to ensure representations and warranties are both broad and precise enough to make up for any lack of due diligence earlier in the process – if drafted correctly the agreement will provide the buyer the opportunity to solicit all relevant information in the representations and warranties, failing which the seller is inviting indemnification claims.

2. Are there any areas of legal due diligence review which are specific to your jurisdiction or which have recently become particularly relevant generally or for certain type of target companies and industries? Is there any regulation relating to the duty of vigilance regarding prevention of occurrence of human rights and environmental risks?

Bulgaria

There are no areas of legal due diligence review that are specific to Bulgaria. This is due to a great extent to the fact that Bulgaria is an EU member and the Bulgarian legislation if fully harmonized with EU law.

We recently see the attention of the potential purchasers focused very much on general compliance matters.

Risk-based analysis and review of potential corrupt practices is carried out in regulated businesses such as businesses in the healthcare, telecoms, and energy industries, as well as in businesses participating in public procurement procedures which account for a great deal of their

revenues generation. Particular efforts are made to investigate potential corrupt practices that may pose a risk under FCPA, U.K. Bribery Act and other anti-corruption laws.

Profound investigation of ownership structure is also very common recently especially where there is no sufficient transparency of the ownership structure combined with indications that sanctioned persons, local oligarchs or politicians may be involved as ultimate beneficial owners of some businesses.

The industry where we see recently many acquisitions in Bulgaria of various sizes is the IT and software development industry. In the course of due diligence review of targets in this industry an extensive review of copyright and other IP matters is carried out together with in-depth employment relations analysis. This is driven by the specific rules of Bulgarian law on copyright as discussed below.

Data privacy is also a hot topic of due diligence review especially in view of the new EU General Data Protection Regulation (GDPR) which aims to harmonize data privacy laws across Europe and to reshape the approach to data privacy. The GDPR will be directly applicable in all EU member states on 25 May 2018 at which time the entities that are non-compliant with the new requirements will face heavy fines.

Another aspect of data privacy in the course of due diligence review is to which extent the target may disclose information to the potential buyer without breaching the applicable data protection rules in the country. In fact there are not specific Bulgarian legislation dealing with this matter but anyone involved in due diligence exercise must determine upfront whether the due diligence investigation may qualify as data processing under the applicable Bulgarian laws and what measures shall be taken in order to make the disclosure of information compliant with those regulations. Such measures include obtaining the consent of the data subjects concerned (which may be difficult to achieve because of practical reasons), finding good arguments to substantiate that the data processing is required in view of the legitimate interests of the data controller and the third persons to whom the data is disclosed, and using anonymised data, etc.

There is no specific duty of vigilance under Bulgarian law regarding the occurrence of human rights and environmental risks but such risks are often subject to due diligence review.

The risks associated with violation of human rights are assessed in view of local laws in the area of protection of human rights and freedoms but also in view of the international treaties on the protection of human rights to which Bulgaria is a party, such as the Convention for the Protection of Human Rights and Freedoms. Particularly relevant in cases of due diligence review are legal risks associated with personal privacy and privacy of correspondence, especially in cases of access to employee's e-mails and other correspondence. Potential discrimination issues under the Law on Protection against Discrimination associated with target's practices and policies are also evaluated in certain instances.

Environmental risks are thoroughly reviewed in the case of acquisition of companies whose activities are of potentially high environmental impact and risk. Environmental risks associated with existing and past contamination by the target of the various elements of the environment and potential exposure to recultivation costs, penalties and/or compensation for damages is usually assessed by a special environmental audit.

France

The number of regulations linked to the prevention of the occurrence of human rights and environmental risks is increasing. In France for example, the Corporate Social Responsibility ("RSE") policy has significantly changed companies' practices.

More recently, the duty of vigilance of parent and subcontracting companies Act dated March 27th, 2017 aimed at parent and subcontracting companies set up a duty of vigilance regarding these issues towards their subcontractors, subsidiaries and suppliers in order to empower big companies and to prevent the occurrence of human rights and environmental risks. This obligation has been codified in Article L225-102-4 of the French Commercial Code which introduces an obligation to establish a system of vigilance (for companies exceeding the threshold of 5,000 employees in the company and its subsidiaries in France or 10,000 employees in the company and its subsidiaries over 2 financial years) with a reporting obligation over the company and its subsidiaries' activities and enforced through sanctions in case of noncompliance.

Poland

Cyber security is an ever-increasing concern of Polish companies but this is no different to other jurisdictions. Although the recent wave of cyber-attacks fortunately did not impact Poland that greatly, it did leave an uneasiness which needs to be addressed in pre-transaction investigations.

Amendments of law also influence the structure of due diligence requests which must therefore be revised constantly. Last year's change in rules concerning transfer of real estate had a big influence on due diligence investigations which concerned entities owning (or having right of perpetual usufruct over) real property classified as agricultural land. Contrary to its seemingly irrelevant impact, the new law directly concerns not only sale of land but also sale of shares in companies, which hold agricultural property. Furthermore, it is deceivingly easy for a company to overlook the fact that at least a part of its property includes agricultural land, as such classification is not obvious.

Regulation (EU) No. 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse ("MAR"), provides the legal basis for changes to disclosure obligations which bind Polish public companies directly since 3 July 2016 - without the need for implementation into Polish law.

Vigilance must be kept at all times in view of current legislative works as these may require paying attention to even more aspects of a target's business.

There are no specific actions have been taken that would impose any need for extra diligence with respect to human rights risks.

Spain

Spanish data protection laws and regulations are very complex and their breach result in the imposition of relevant sanctions.

Also, due to the extraterritorial nature of the application of laws for the prevention of fraud, bribery and corruption, the due diligence of Spanish companies with cross-border activities is also starting to focus on these matters.

Finally, there is no specific regulation relating to the duty of vigilance for the prevention of the occurrence of human rights and environmental risks.

USA

One of the most quickly developing and expanding areas of due diligence in the US currently is cybersecurity due diligence. As is evident each passing day with constant news of ransomware attacks, large-scale theft of proprietary information, and other data breaches, the risk to businesses large and small, at a global level, is increasing with no end in sight. The situation is complicated by the fact that the average time between a breach and its discovery is over a hundred days, and a problem may only be discovered after an acquisition closes.

Moreover, businesses in almost all industries are more dependent upon sophisticated information technology, which results in vulnerability to attacks.

Accordingly, it is incumbent upon an acquirer to carefully vet a target's situation in regards to data privacy and security. The extent of the risk and corollary scope of due diligence will depend upon several factors, including:

- the extent to which the target possesses or uses personal information, personally identifiable information and/or financial information of its clients;
- the extent to which the target possesses or uses more highly regulated types of customer information, such as health care related information, which are subject to additional protections;
- the extent to which the target possesses sensitive trade secrets;
- the scope of the target's reliance on information technology systems in operating its business and the likelihood that an interruption of those systems would be damaging to its business.

The due diligence requires the collaboration of legal and technical experts and will investigate, among other things:

- the target's policies and procedures to protect data and privacy;
- the target's compliance with its own policies and procedures;
- the target's compliance with relevant laws and regulations;
- the quality of the target's information systems controls and their compliance with best practices;
- contractual protections in favor of the target in its agreements with third party vendors who have access to any of the types of information described above.

As regards environmental and human rights concerns, the topics of environmental law and employment law due diligence regularly form part of a buyer's overall due diligence, and the scope of that review will vary heavily depending on the nature of the target's operations. For businesses own or use real estate, as opposed to relying primarily on intellectual capital, environmental due diligence can be of paramount importance. There is not a focus on human rights as such in the US, the issue, if any, will be of any liability for past misconduct.

3. Do you see any recent trends in setting materiality threshold levels in legal due diligence review? How are materiality thresholds defined and what do they depend on?

Bulgaria

Materiality thresholds are getting higher especially in multi jurisdiction acquisitions where the Target has operations and subsidiaries in many countries. For most of the clients there is a level of materiality below which due diligence findings are unlikely to justify the cost of due diligence review. Thus the local operations very often fall fully or partially below the radar.

It is also very common to apply a sampling approach to the review of particular type of documents in the course of legal due diligence review which in certain cases poses the risk of missing material legal issues. Particular example of such sampling approach is the review of randomly selected credit files, title and lease documents relating to the retail network in most of the cases of due diligence review of financial institutions.

Materiality thresholds usually are set by the client and depend on the size of the transaction while they vary widely and we may not quote a percentage of equity valuation as the average materiality threshold in deals in Bulgaria or the region. It is worth mentioning that this criterion is very often combined with other criteria which are more general and aim to catch any legal document that might be material to the business or to the transaction.

France

In order to limit the costs spent on the due diligence review, the level of materiality thresholds are higher than they used to be. Clients are more and more looking for big risks. The materiality thresholds are defined with the client on a case by case basis and depend on the target's size, the activity or business volume.

Poland

Materiality thresholds have become a norm in preparing for and conducting a due diligence review. Usually set by clients, they are also used by law firms to specify the scope of their review and to adjust it to clients' increasing needs to keep the process high level and short. This practice is generally in lines with clients' approach to the analysis, the objective of which usually serves to acquire a general perspective of the target and a more in-depth view only of its most significant activities.

With large targets that are parties to thousands of customer contracts, it is the norm to either set threshold on the value of the contract or to otherwise limit the number of examined agreements to e.g. top 10% customers. There is no common value of the threshold for all investigations - this usually varies from EUR 50,000 to EUR 500,000 and usually depends on the value of the target business.

Spain

Materiality thresholds are defined with reference to the value of the target business. Usually, the *de minimis* amount that is included in the provisions of the sale and purchase agreement governing the seller's liability is equal to the materiality threshold taken as reference for the due diligence review.

USA

Thresholds for disclosure can vary greatly depending on the nature and size of the target's operations.

Monetary thresholds are sometimes helpful but often belie more sensitive notions of materiality based on the potential impact of an event to the operations of a company, and are, therefore, often avoided for various types due diligence inquiries.

Nevertheless, the "business team" working on a transaction involving sophisticated parties will regularly have its own definitions of what it considers to be material, at least from a monetary perspective, and that will often inform and guide the process - especially in financial and valuation-related inquiries.

4. What type of due diligence report you are more often requested to prepare red flag or full report summarizing documents reviewed? How has this process changed in your jurisdiction in the past 10 - 15 years?

Bulgaria

Over the past fifteen years the client's preferences evolved from full descriptive due diligence reports into key issues type of due diligence reports. In the past we were more often requested to provide full summaries of documents reviewed than nowadays. These days in the rare occasions when we are asked to prepare summaries of documents reviewed it is rather an outline of specific terms and conditions of contracts and other legal documents which are particularly relevant for the transaction or for the post-acquisition integration process or a high profile summary of source documents which are available for review only in Bulgarian.

Recently we are requested to prepare red flag reports highlighting key legal issues and legal risks and assessing their impact on the valuation of the target, the transaction structure, the transaction documentation and the post-acquisition integration, if applicable. Full reports summarizing legal facts and documents are very rare but are sometimes prepared for the purposes of vendor due diligence reports to be released to potential bidders in structured auction processes.

France

10 – 15 years ago, due diligence reports were very extensive. They described the situation of the company or group of companies from a legal, tax and labour standpoint and indicated the risks when identified.

We now provide clients with red flag reports, only stating the risks identified (potential occurrence and financial consequences for the company - when possible), legal sanction, and recommended ways to remedy the risks or deal with them through the representation and warranties for example.

Not only the length has changed but also the format. Our report changed from Word documents to PowerPoint slide packs presentations summarizing in bullet points, charts or diagrams any concept which may be most easily understood in this form rather than sentences.

Poland

Long gone are the days of organized excursions to the seat of the target to go through endless folders of documentation and hour long interviews with company staff. Nowadays the norm is a virtual data room and centralized Q&A process, often with strict limitation as to the number of questions that may be posed to the target. Today clients usually want to receive a concise red-flag report indicating only the significant risks, although at the same time they do appreciate an additional section providing additional comments on noteworthy aspects of the target's activities.

Very rarely are Polish lawyers requested to provide the voluminous, detailed reports, which were a norm 10 - 15 years ago. If this does happen, it is usually requested by a sector investor entering our region of the world for the first time and wishing to get a better understanding of the details of the business from a Polish perspective.

Spain

Currently, we are more often requested to prepare red flag due diligence reports, as opposed to descriptive reports summarizing documents reviewed. However, in certain transactions (for example, those involving the acquisition of a business highly dependent on certain software or technology) the due diligence report may include a contingency / risk analysis and a descriptive summary of certain key areas.

This has been one of the fields where due diligence has most evolved in the last decade. We are also experiencing a change in the way reports are presented to clients (executive summaries, visual and graphic elements, etc.).

USA

The type of report requested or expected depends to a large degree on the institutional philosophies and experience of the buyer, the size of the transaction and complexity of the target's operations.

Some buyers prefer detailed reports of substantially all due diligence and others are only concerned with "red flag" reports. Others still will expect detailed summaries of certain due diligence materials, such as lease abstracts, summaries of litigation, and environmental issues, and rely on more limited summaries of other types of information such as with respect to contracts, in which any consents to be obtained in order to close must be identified.

Needless to say, transaction counsel should consult with their clients to ensure client expectations are known before the process begins.

There has always been significant variance in the expectations of clients as to due diligence reporting, but in the past 10-15 years, particularly with large buyers who have full-time in-house teams of transactional staff, there are more examples of transactions in which much of the due diligence review process is taken care of internally, while outside counsel will be asked to consult on high-risk or highly critical issues.

5. Due diligence then and now - how has the process changed in your jurisdiction in the past 10 - 15 years? In your experience, to what extent does the due diligence exercise in your jurisdiction differ materially from practices in other jurisdictions, and why?

Bulgaria

The standards for due diligence review are pretty much harmonized across Europe and also in the CEE and SEE region while taking into accounting the specifics of the target and the industry in which the target operates. Thus legal due diligence exercise in Bulgaria is carried out in line with best practices in Europe and does not materially differ from such exercise in other jurisdictions which is clearly seen in multi jurisdiction due diligence exercises covering a target operating globally or regionally, including in Bulgaria.

It is worth mentioning that some Bulgarian sellers and targets do not understand the need of full disclosure in the course of transaction due diligence and withhold documents or disclose many documents which are business sensitive in their view at a very advanced stage of the due diligence process or immediately before signing of the SPA with the disclosure letter which creates complications in the transaction process.

France

Data rooms went from physical to virtual and interviews of the management from meetings to conference calls or video conferences. The process is more standardized therefore allowing due diligences review to be organized for group of companies having entities over different jurisdictions with the same process and the results to be obtained quicker.

Poland

It doesn't seem that Polish due diligence reviews differ greatly from those conducted in other European jurisdictions. On the one hand the process has become easier as documents are made available on line in virtual data rooms and there is no need to travel to conduct onsite visits. However, at the same time scrupulous investigation of the company and interviewing local staff is not possible and full understanding of the business is more difficult. Lawyers rarely have full access to local management and are often requested to limit the number of questions asked.

Spain

In the past 10-15 years the logistics of the due diligence have changed. Lawyers no longer need to travel to a data room, where dozens of boxes are waiting them full of documents, with limited access hours and where only one lawyer can review a document at a time. Currently, due diligence is conducted in a more efficient manner through virtual data rooms that avoid travel time, allow continuous access throughout the day and do not limit the number of lawyers that can review a particular document at the same time. Virtual data rooms also offer different options to access the documents, that may be customized by the seller (view only, or view, download and print). Turning to the second part of the question, Spanish due diligence reports provide a more detailed legal and case law analysis as opposed to the reports of other jurisdictions, that do not provide such detailed analysis.

USA

The legal profession in the United States presents a unique characteristic compared to many other jurisdictions, especially some in Europe, in that lawyers in private practice in the US practice in firms that, for reasons based on the existing rules of professional conduct for attorneys, prohibit the ownership of firms by non-lawyers. Accordingly, whereas in numerous other jurisdictions, accounting, legal, and other professionals are partners in a single firm, that is not the case in the US.

From a transactional perspective that means that there is almost always a law firm and separate accounting firm involved for each party in the transaction, whereas, all due diligence might be handled under a "single roof" in other jurisdictions.

This is not of any particular concern, and US transactional lawyers and accountants are quite experienced working together on due diligence and other aspects of a deal, however the potential efficiency of having a single firm handle the entirety of a matter that may exist in other jurisdictions is not something available here.

6. What are some of the pitfalls to watch out fall while doing due diligence in your jurisdiction?

Bulgaria

The pitfalls to watch out for widely vary target by target.

Still it is worth mentioning that title due diligence with respect to real estate in Bulgaria is challenging due to the complicated legal regime of owners registration and the outstanding risk of pending restitution claims. The Bulgarian Real Estate Registry is a registry of events affecting legal rights (i.e., agreements, encumbrances, statements of claim, etc.) but not a registry of legal rights. There is no rule that the latest registered transferee of a piece of real estate is considered the owner of the allegedly transferred real estate. To ascertain the legal rights of a registered transferee, one must follow the chain of registered transactions/events back in time, until one comes to a fact/circumstance which would be of a nature to confirm that the latest transferee acquired title as a result of the registered transfer. Therefore, a transferor with undoubted rights must be discovered down the chain of title, or a period of adverse possession which is sufficient to constitute title.

Another challenging area of due diligence under Bulgarian law that is especially relevant in cases of acquisition of IT and software development companies is copyright. Under Bulgarian law copyright in software and databases developed by the employees of an employer arises for the employer, unless otherwise agreed between the parties. Under Bulgarian law, with respect to the different types of works (other than software and databases), the employer is granted a statutory right to use such works in the course of its customary business activity, whereas if broader rights are necessary, such effect may be achieved contractually. However, transfer of copyright is not allowed under the Bulgarian law and in view of this any agreement on the transfer of copyright in works is not valid. Accordingly, the broadest scope of rights that may be acquired by a person not initially vested with the copyright are on grounds of a license to use such works, whereas the licensee's rights must be worded as broadly as possible.

According to Bulgarian law (which is applicable to determine the transferability of copyright that has arisen in Bulgaria) copyright may be only licensed. The transfer of economic rights and part of the moral rights in copyright protected works is not permissible under Bulgarian law. This restriction comes from Bulgarian legal doctrine and there is no sufficient court practice on the matter. Furthermore, as a matter of conflict of laws rule transfer of copyright is regulated by the law where protection of the copyright is sought. Given that different national legislations treat the possibility for transfer of copyright differently, cascade vesting of rights is often recommended to contracting parties in the case of intended transfer of copyright on software developed in Bulgaria, i.e. the parties to agree that if and to the extent that a transfer of copyright is not permitted by the applicable law, a license for the copyright is considered agreed. The maximum

statutory license term for a copyright license under the Bulgarian law is 10 years and there is no prohibition on renewal of the license term for further maximum periods.

Specific due diligence effort shall be also made to confirm transferability and change of control requirements related to local permits and licenses issued by the competent regulatory authorities in regulated industries.

France

We do not have any particular pitfalls in France. On a general point of view, the most important difficulty is to meet to client expectations (secure the deal and raise main findings) in a very tight time frame with lower fixed fees. Tax and labour law in France are amended on a yearly basis. Even if the client consider due diligence review as a very routine work, this is not the case. Lawyers have to be updated on those changes.

We are not selling documentation but solutions.

Poland

It does not seem that the Polish due diligence process differs greatly from others performed in the region or even in Europe in general. An issue that needs to be considered in each case is whether are any public entities are involved. If so, requirements imposed by the new MAR provisions must be observed and members of the due diligence team will need to be made aware of them.

Spain

Nothing specific relating to Spain. As in other jurisdictions, certain areas require due diligence over legal, technical and economic aspects (for example, town planning, environmental, finance). Law firms need to be aware of this, occasionally work alongside experts in these areas (with the knowledge and understanding of technical matters that this requires) and be ready to advise the clients on the need to engage these experts.

USA

Due diligence is a task that must be conducted carefully. The purposes of due diligence are central to a buyer's transactional goals, such as:

- ensuring it is acquiring what it expects to acquire;
- confirming the value it has placed on its acquisition;
- ensuring it understands any problems or risks associated with its target;
- allowing the transaction team to structure or restructure the transaction to minimize risk;
- depending on the nature of the buyer, understanding the industry it will be entering.

Failure to identify problems that would affect any of these central goals could imperil the buyer's investment or result in other problems down the line. Accordingly, attorneys must understand expectations early, be attuned to the client's concerns, and be on the lookout for issues that might adversely affect the transaction.

7. What is the impact of the business culture in your jurisdiction on the accessibility of information necessary to perform proper due diligence? What steps do you take in order to overcome these barriers in your jurisdiction?

Bulgaria

We usually experience difficulties in convincing small and even medium sized businesses to make full disclosure of requested due diligence information even in cases where it is protected by an executed non-disclosure agreement. Sellers are very often afraid of access to sensitive commercial information by competitors, rumours on the market that may impact the market position of their business as well as their customers' loyalty and the commitment of their long-term employees.

Very often we need to educate the sellers and even the legal advisors of sellers who do not have sufficient experience as transaction lawyers on the need and purpose of the due diligence exercise and the disclosure process.

More sophisticated large businesses are much more straightforward and transparent in the process of due diligence especially when they are willing to do the deal. Still they are very much concerned about leakage of trade secrets and sensitive confidential information.

Poland

It is impossible to generalize this issue and it depends rather on the type of business involved in the transaction and not all of the business culture in Poland. If asked about the overall level of willingness to share information with lawyers it must be said that this is not very high. Companies are reluctant to provide all the documents we ask for. However, we find this to be usually true for all jurisdictions with which we come across during transactions. One aspect that may differentiate Poland from other jurisdictions is the investigation of title to shares. Under the Polish law, it is necessary to conduct a thorough review of all documents encompassing all historic transfers of shares. This is due to the fact that entries in the trade register do not enjoy protection of certainty of law (as is the case for real property and entries in the land and mortgage register). In other words, there is no guarantee that the disclosed shareholder holds undisputable title to the company's shares. If any of the past transactions was not performed correctly, all subsequent transfers were invalid. This is not an easily curable issue. Consequently, Polish lawyers spend a considerable number of hours repeating requests for share transfer documents which were produced many years ago and which preceded several later transactions.

The issue is more problematic in transactions, which include the sale of family businesses. It is very difficult to convince the sellers to disclose sensitive information to potential buyers and a lot of effort is usually put into discussing ways to give the parties comfort. A common remedy is to provide a limited set of information (redacted contracts or generalized sales data without indicating specific contractors) in an initial due diligence and subsequently disclosing more or all details once a signing takes place and a supplementary due diligence is performed.

Spain

Usually, management understands that proper due diligence requires full disclosure of all the relevant information. In certain sensitive areas, key information is disclosed at a later stage in

the process, or third parties independent from the seller and the purchaser are engaged to provide confirmation on certain matters without disclosing them to the purchaser.

USA

For the most part, and certainly where sophisticated parties are involved on both sides of a transaction, due diligence is a known and expected part of the transaction process in the US meant to facilitate a transaction's completion. Accordingly parties are customarily cooperative and bring to bear the necessary resources to ensure the process is smooth and efficient.

It may occur, notably in circumstances in which the Seller's counsel and other advisers are less acquainted with or experienced in the M&A process, that logistical impediments or lack of cooperation delays or impedes due diligence. In such circumstances, in coordination with the buyer, it is sometimes necessary to reiterate to seller and its counsel the significance of the review and insist on receipt of all requested information.

Ultimately, an honest-dealing party desirous of consummating a transaction will usually cooperate. Hindering a diligence investigation may open the Seller to fraud claims post-closing should problems arise.

Sometimes, a seller will be reticent to disclose information, which if leaked, could adversely affect the business prior to closing (for example, by flight of employees or customers). In such circumstances a buyer might accommodate the concern and accept lighter due diligence in anticipation of executing an agreement, but in return would require a much more meaningful condition as to satisfactory due diligence, which ironically, could result in the same issues the seller was attempting to prevent in the first place.

8. Are there any specific problems (e.g., occupational safety/health, environmental compliance, corruption) in companies in your jurisdiction that can be particularly damaging to a company's reputation and should be taken into account when conducting due diligence? Is it usual to engage consulting firms to perform non-legal due diligence related to environmental, compliance, tax, etc.?

Bulgaria

Compliance has become hot topic everywhere and clients are becoming more and more focused on compliance matters in the course of due diligence. We often see profound compliance due diligence being carried out in parallel with legal due diligence.

Corruption in Bulgaria is particularly relevant issue for certain regulated businesses and such relying for their revenues generation mostly on public procurement. We are sometimes asked to carry out legal review of forensic reports prepared by other service providers on certain practices in which the client sees the risk of potential corrupt practices.

We often advise our clients to carry out together with legal due diligence environmental audit in order to identify environmental risks, environmental damages, potential penalties and costs for remedial actions with respect to targets in industries where the environmental risk is potentially high.

As a matter of rule financial and tax due diligence is carried out by respective financial and tax consultants in parallel with legal due diligence.

France

Corruption, remuneration of the managers and tax issues have been damaging to companies' reputation. However up to recently these reputational damages concerned only big companies.

In the coming years these issues will concern more companies as the same legislation is progressively applying to companies of smaller size. In addition new laws are also being passed in these areas. For example, the Sapin II Act dated December 9th, 2016 has introduced new regulation on corruption and provides for new obligations for companies to implement measures and procedures for detecting and preventing bribery and influence peddling (internal whistleblowing system, risks mapping, accounting procedure disciplinary systems, control mechanisms, internal evaluation, etc.). Compliance with such obligations should be part of our scope of review and as such should be included in our reports.

It is usual in France to engage consulting firms for environmental and health and safety issues. The lawyers of our team specialized in these areas review the legal aspects and work hand in hand with specialized consultants for the technical part of the audit. Technical audits go from a review based on documents (phase I) to the analyses of samples (phase 2).

Poland

Reputation is very important for businesses in today's highly competitive market. That is why they are becoming more and more careful not to allow any unexpected circumstances to threaten their position. This is one of the reasons why, more and more often, management boards are ordering an increasing number of internal due diligences reviews. The reason for these investigations is not connected with any contemplated transactions but with the need to assess the company's compliance with binding rules and regulations the number of which increases very rapidly making it difficult to follow all obligations.

Spain

As mentioned above, fraud, corruption and bribery are areas of particular relevance these days. These practices can risk the target's reputation not only in its jurisdiction, but also abroad, due to the extraterritorial nature of the laws and regulations enacted to prevent them.

In Spain, as well as in other jurisdictions, it is usual to engage other experts to perform non-legal due diligence regarding technical matters (zoning and town planning, environmental, finance and tax, hazard prevention, etc.).

USA

Significant legal violations, major litigations, allegations of wrongdoing or illegality and issues of that nature are susceptible of being of particular concern to a buyer. Obviously the magnitude of a problem can vary greatly depending on the size of the target and the transaction. Moreover, allegations are not always true and explanations exist for various issues that, at first, may seem concerning. Accordingly good communication with the client and between the buyer and seller teams is critical during due diligence so issues can be brought to light and thoroughly examined so the parties can make fully – or as close as possible to fully – informed decisions.

It is customary to have a team of experts participate in due diligence, including counsel with expertise in the relevant subject matter and non-lawyers alike.

For example, in addition to transaction counsel, the legal due diligence team will, depending on the nature of the transaction, often include counsel whose expertise is in:

- Tax law
- Environmental law
- Litigation
- Real estate law
- Labor and employee benefits law
- Intellectual property

Moreover, outside non-legal consultants will include any or all of the following:

- Accountants, appraisers, and/or auditors
- Environmental consultants
- Human resources consultants
- Insurance consultants

Additionally, in the event of a transaction with a cross-border, international or multi-jurisdictional component, counsel and any or all of the other foregoing practitioners may be required in multiple jurisdictions.

Finally, it is increasingly common for buyers astute to the issue of corporate culture and corporate integration to engage consultants who will evaluate corporate integration challenges and make recommendations for a successful post-closing.

9. How has the approach of clients and law firms changed to issue of liability for performing the due diligence? What is the approach depending on the type of due diligence performed (vendor due diligence, buyer due diligence, due diligence for ancillary jurisdictions)? What is the position of your firms should the client ask you to amend the VDD i.e. not to disclose certain findings?

Bulgaria

Bulgarian law firms do not usually limit their liability for legal due diligence review and reports provided to their clients either on the sell or on the buy side of a transaction.

In cases of multi jurisdiction due diligence carried out by different law firms in different jurisdictions it is important for local law firms to clearly define scope of due diligence review and reporting and to limit liability to such scope of review and reporting especially when they are not the lead counsel on the transaction. In such cases it becomes very important to avoid aggregate liability caps, if applicable, and to cap liability separately.

Upon client's request purchaser due diligence report is usually released on full reliance basis to co-investors, to financial institutions providing acquisition financing as well as to insurers providing R&W insurance.

On the other hand the issue of limitation of liability of law firms when performing due diligence has recently become particularly relevant with respect to vendor due diligence reports released on non-reliance, or in certain cases on reliance, basis to bidders in structured auction processes.

Recently in Bulgaria as a matter of rule vendor due diligence report is prepared by the sellers in cases of structured auction processes and the vendor due diligence report is released to bidders for review on non-reliance basis. In certain cases reliance is provided to the winning bidder subject to certain qualifications relating to the scope and purpose of the vendor due diligence. In such cases liability of the law firm that prepared the vendor due diligence report is usually capped at some level usually linked to the professional insurance coverage of the respective law firm. Limitation on liability in Bulgaria does not work in cases of gross negligence and wilful misconduct.

We as a firm have been asked occasionally to amend a vendor due diligence report by omitting sensitive legal issues analysis before such report is released to the bidders in a structured auction process. We usually resist to this approach as far as the quality of legal risks analysis may be compromised. Still, in certain cases we prepare on demand and in addition to the vendor due diligence report which remains undisclosed a tailor made vendor due diligence report, or legal section of the information memorandum, or legal facts sheet containing an outline of legal facts and issues related to the target while making a specific disclaimer that it shall not be considered a full-fledged legal due diligence report as it does not contain detailed analyses of such legal facts and issues, the legal risks associated therewith and potential remedies.

France

Clients want to spend less fees on due diligence reviews. In order to be more efficient and profitable on due diligence reviews law firms tend to limit their review to the documents provided by the seller(s) (whether it be for buyer-side or seller-side deals). Disclaimers become an important part of the due diligence exercise. The risk of this approach is to miss an important issue.

In France, this risk should now be more limited as French law has just been modified recently (contract law reform which came into effect in October 2016) and now imposes on the seller or the buyer to disclose to the other party any fact which would be considered as of ''decisive importance'' within the meaning of article 1112-1.al.1 of the French Civil code ("*The party who knows information which is of decisive importance for the consent of the other, must inform him of it where the latter legitimately does not know the information or relies on the contracting party"*).

Any request by a client to amend the report in order not to disclose certain findings would be turned down. Solutions to remedy the risk may be presented or evaluated, impact on the price may be negotiated but Fidal will not endorse the liability of hiding some information from its report.

Poland

It seems there is an increasing trend to demand law firms to issue release and reliance letters. This is a norm for transactions, which involve banks but can also happens if there are other

entities involved in the transaction which are not directly connected on a client-attorney basis with the law firm. Considering the previously mentioned pressure to limit scope and time spent on due diligence review law firms are faced with the difficult task of including language, especially in reliance letters that will limit their liability towards anyone who wishes to rely on due diligence reports.

Clients may request that certain issues raised in a due diligence report be presented in a less harsh manner and if such change does not distort our assessment of such issue we are ready to discuss the matter with the client.

Spain

There is always a debate between the liability that a law firm is willing to assume as a result of a due diligence and the one that the client or third parties are expecting the firm to assume. This debate is of particular relevance in the case of vendor's due diligence, where the addressees of the report (the potential purchasers) are different from the client. In these instances, law firms in Spain tend to limit their liability with reference to the fees incurred in the due diligence exercise, as opposed to being exposed to unlimited liability. Sometimes, the final purchaser may request a reliance letter from the law firm that prepared the vendor's due diligence report, whereby the law firm assumes liability *vis-à-vis* the purchaser in connection with the content of the due diligence report.

From my experience, we have never been requested by a client to withhold certain information. This will certainly expose the firm to liability and, therefore, would not be an appropriate practice. In the context of vendor's due diligence, we usually reserve our right to amend and update the report prior to signing the SPA if we uncover certain facts that are not disclosed in the report delivered to the potential purchasers. Sometimes, this results in a conflict between the client and the firm, since the client may prefer not to disclose certain information at an advanced stage to avoid the risk of further negotiations.

USA

Attorneys owe their clients a duty of professional care. This duty of care requires attorneys to perform their legal work for their clients diligently and with good faith.

The standard that has been applied to determine whether an attorney fulfilled his or her duties is whether the attorney exercised ordinary reasonable skill and knowledge commonly possessed by a member of the legal profession.

In the context of due diligence this means that an attorney is required to conduct the process with reasonable knowledge and skill. When staffing a due diligence team, it is advisable to make sure that the attorneys who will be performing the review understand the transaction, the client's needs and goals, and any special types of risk that are in focus, and to clearly communicate findings.

Since prompt and clear communication of issues are very important in protecting a client, it is always beneficial to emphasize that reviewing attorneys communicate regularly with the senior attorneys managing the transaction to keep them apprised of findings in real time. Importantly, lawyers should only be conducting due diligence within their competency, and of course, only legal due diligence. Additionally if there are any intended limitations to the scope of due diligence, they should be specified in advance in an engagement letter with a client.