



COMMERCIAL DUE DILIGENCE

ICAEW CORPORATE FINANCE FACULTY
BEST-PRACTICE GUIDELINE 72



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FOREWORD AND ACKNOWLEDGEMENTS



Understanding the market in which a business operates and the assumptions that drive its business plan and projections are vital parts of any investment decision. Commercial due diligence enhances that

understanding and is the subject of this guideline from the Corporate Finance Faculty, co-authored by member firms KPMG and Luminii Consulting.

With product and brand life cycles becoming shorter in some markets, and the use of AI playing a part in both shaping and monitoring consumer demand, commercial due diligence has never been more complicated, or more important. The guideline has been written for use by many different parties to a transaction, including, but not limited to: principal investors, in both private equity and corporates; lead advisers; banks and providers of private capital; lawyers and other providers of various forms of due diligence.

The faculty would like to thank Edward Ataii, David Larsson, Yuan Zhang and their colleagues

from KPMG, and Lushani Kodituwakku, Ioana Nobel, Sam Thompson and their wider team at Luminii Consulting for their enthusiastic and expert development of this publication. My thanks also to my colleague at ICAEW, Katerina Joannou, for collating the guideline and taking into account comments from many of our member firms.

All our best-practice guidelines are subject to rigorous peer group review co-ordinated by the faculty's technical committee. While the content reflects the views and experience of its authors, it is also aligned to practices at leading member firms. These guidelines, therefore, represent market 'best practice'.

I hope you find this guideline thought provoking and useful, and that lead advisers refer to it when considering matters such as setting the scope of an engagement. For principal investors, it may even ultimately prove useful when considering the \$64,000 question – whether to invest at all.

David Petrie

Head of Corporate Finance, ICAEW

INTRODUCTION

Commercial due diligence (CDD) is an important component of the investment appraisal process for organisations considering an acquisition or divestment.

The CDD process helps prospective investors by:

- providing an enhanced understanding of the target entity's market environment, competitive position and customer retention;
- offering an independent critique of the key assumptions in the target entity's business plan, thereby helping refine the valuation; and
- acting as an important input into the value creation plan for the investment.

In this guideline, we explore the roles and responsibilities of the various parties within a CDD process, as well as the impact of artificial intelligence (AI) and other tools on the process itself. The guideline sets out best practice for CDD on sell-side and buy-side transactions and has been authored by experienced CDD practitioners.

Types of due diligence

CDD is only one type of due diligence. There are many other types, such as financial, legal, operational, management, technology, tax, environmental, social and governance (ESG), intellectual property (IP)



ICAEW fundamental principles

This guideline frequently references ICAEW's fundamental principles: integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

ICAEW members are required to comply with these principles, together with the specific requirements of ICAEW's Code of Ethics, in their professional and

and HR/pensions. Some types of due diligence will cross over and inform other areas. In some cases, purchasers may seek to commission CDD ahead of other due diligence work to gain an understanding of the market, and key growth opportunities and risks, before committing to further consideration of the target entity and significant deal costs. This is expanded upon in section eight.

Intended audience

This guideline is primarily aimed at CDD practitioners and those commissioning CDD services but also includes considerations for management teams that are the subject of a CDD exercise. It aims to provide insights into the key principles, best practices and emerging trends that can enhance the quality and effectiveness of the CDD process, and ultimately an understanding of how CDD contributes to the investment decision-making process.

Main audience groups:



The CDD practitioner and other transaction advisers



A potential purchaser or lender



A business in a transaction situation

business activities. In due diligence engagements, managing conflicts of interests, protecting confidential information and demonstrating objectivity are particularly pertinent.

To provide clients with quality advice, it is also essential that the CDD practitioner has appropriate professional competence and exercises due care. See the table on page 7, which illustrates the relevance of the principles to the CDD proposition.

SECTION

1

CDD EXPLAINED

What is CDD?

CDD is typically undertaken in connection with a transaction, covering situations such as acquisitions, mergers, capital raises, management buyouts (MBO), leveraged buyouts (LBO), refinancings or restructurings.

A CDD exercise is an objective enquiry to critique and challenge commercial matters relating to a target entity, including its business plan and financial projections. The CDD practitioner would normally comment on a target entity's market and competitive position as well as the potential for future revenue growth and margin expansion. This commentary is based on evidence developed through analysis of market, competitor and customer information, as well as analysis of the target entity's business model and financial and commercial performance. The information used for this exercise is obtained through a range of sources, both internal and external. The practitioner will also seek to identify key risks and opportunities and offer recommendations to mitigate the risks and enhance value creation post-investment.

In an acquisition context, the primary purpose of CDD is to help inform the purchaser or lender, with the CDD practitioner's commentary used to support their 'go' or 'no-go' investment or lending decision. Additionally, the CDD findings can often influence deal terms and valuation adjustments and help inform the purchaser's 100-day plan and post-deal strategy.

CDD does not constitute an audit or review under any assurance standards and, therefore, no formal opinion or assurance is given.

Forms of CDD

As with other types of due diligence, there are several forms CDD can take, depending on whether it is commissioned by the seller, purchaser or lender and the extent of due diligence required. While there are some areas which CDD would normally be expected to cover, CDD scopes are never pre-determined but need to be adapted to each situation.

Buy-side CDD

In buy-side CDD, the scope and format of the report are determined by the prospective purchaser or lender commissioning the work and tailored to address their specific needs and most important commercial questions.

The scope will also be impacted by access to the target entity, available information and project timeline.

However, some of the broad categories of CDD scope generally recognised by market participants include:

→ **full scope CDD.** This is a more comprehensive due diligence exercise that typically focuses on the key commercial assumptions included in a target entity's business plan, covering all or most aspects of the CDD scope of work (see section four) based on in-depth analysis of the findings from extensive primary and secondary research. The analysis and the evidence supporting the recommendations are set out in an extensive report. See sections six and seven.

→ **limited scope CDD.** This is often conducted in the context of a smaller investment or where the bidder is confident they can address wider commercial questions without external support. The scope may deliberately be more focused due to the proportionate cost of engaging external advisers, or when the purchaser already has an understanding of the industry in which the target entity operates, for example a private equity firm with a previous investment in a sector, or a corporate acquiring a competitor. This streamlined form of CDD typically concentrates on specific areas, such as customer referencing, market sizing or competitor benchmarking, which may be conducted as standalone components. It is also often commissioned by venture capital firms when providing growth capital for early-stage businesses or smaller transactions, where the overall deal value does not justify a comprehensive due diligence budget.

→ **red flag CDD.** This is normally an early stage, high-level or focused due diligence exercise designed to raise more critical risks or red flags in specific areas. It is typically undertaken where:

- a prospective purchaser quickly wants to identify potential deal-breakers or key areas of concern before they decide to progress the deal and undertake further due diligence. For example, if it is already known that customer concentration is a key risk, the CDD could involve early interviews with customers to consider the longevity of the target entity's revenue streams; and/or
- there are time constraints within a deal process, which limits the ability to conduct full scope CDD.

A red flag CDD can often progress to a full scope CDD in subsequent phases if the prospective purchaser deems the risks identified in the red flag process to be manageable and they still want to pursue the transaction but require further due diligence.

→ **top-up CDD.** This is a supplementary due diligence process generally commissioned by a prospective purchaser when a vendor-initiated CDD (V-CDD) report has already been prepared (see below). The top-up CDD covers any perceived gaps in the V-CDD. It addresses specific purchaser concerns that have arisen during the deal process and considers more detailed, targeted or recent information.

Vendor-initiated CDD (V-CDD)

A V-CDD exercise is commissioned by the seller of an entity to provide prospective purchasers with a CDD report. The scope of work is designed to be closely aligned to what a typical purchaser would request if they were commissioning the V-CDD report themselves. This means that V-CDD reports generally tend to be reasonably comprehensive in scope for the specific transaction and typical purchaser. However, it does not always go into the required detail in every area for all bidders, who would then commission top-up CDD work. While the seller commissions the V-CDD engagement, the actual purchaser (and parties connected with the purchaser, such as lenders to the transaction) or the actual lender (in the case of refinancing) are the addressees or beneficiaries of the V-CDD report.

The benefits of V-CDD include:

- rapidly and objectively addressing matters that are commercially important to prospective purchasers

early in the sale process. This is particularly important where the target entity operates in markets that are not well understood, or are subject to significant uncertainty.

- widening the pool of prospective purchasers, who may otherwise not consider the opportunity.
- helping to avoid unforeseen due diligence issues and surprises (for both the seller and prospective purchaser) later in the transaction process.
- offering the seller greater control over a streamlined transaction process.
- avoiding the disruption of multiple parties undertaking CDD and reducing the number of explanatory questions the seller needs to respond to. It ensures that all prospective purchasers have a minimum level of understanding of the target entity.
- improving the consistency of transaction documentation, for example by ensuring that the information memorandum is not inconsistent with the V-CDD findings.

Timing and duration

Similar to other types of due diligence, the timing of the CDD work varies depending on its form and purpose (for example, buy-side vs vendor-initiated). As explained in further detail in section five, buy-side CDD can be performed at various stages of the deal process, such as initial red flag CDD or limited scope CDD in round one and more comprehensive or top-up CDD at a later stage.

The duration of the CDD process is influenced by several factors, including the breadth and depth of the scope of work, as well as the geographic coverage, as discussed in section four. As a general guideline, a typical CDD engagement can take approximately three to six weeks, but in some cases can be considerably longer.

The extent of the primary research undertaken also has an impact. Where extensive customer referencing, surveys or interviews are required, the timing and duration will also depend on the target entity facilitating introductions to key stakeholders (such as customers, suppliers and prospects), and the availability of those interviewees. These logistical elements can significantly impact the overall CDD timetable.

SECTION

2

COMMISSIONING A CDD ENGAGEMENT

Commissioners

Typically, CDD is commissioned by:

- **financial investors.** These include private equity, funds (infrastructure, pensions etc) and venture capital firms. Financial investors will commission CDD when they are looking to make an investment or divestment of one of their portfolio companies. Within these institutions, CDD is typically initiated by investment teams (including investment partners, directors and associates) and may be a requirement for an investment to be formally approved by an investment committee.
- **corporates.** They may commission buy-side CDD for acquisitions and V-CDD for divestments (or in connection with the refinancing of private debt facilities). CDD is usually commissioned by senior executives, including the chief executive officer (CEO), chief financial officer (CFO), the mergers and acquisitions (M&A) team, or at the instruction of the board. Larger corporates may have internal M&A or investment teams that will conduct some

due diligence in-house, particularly if the target entity operates in sectors that are well known to the organisation. However, it is common for external advice to be sought for transactions that involve new sectors, for particularly large or high-risk investments, or where in-house capability or capacity is insufficient. If a business wants to list its shares on the public markets, it may commission CDD, depending on market practice and the needs of sponsoring banks. The CDD report prepared in this situation would still be a private report – neither the report nor the preparer would usually be referenced in the public offering document.

- **debt providers.** When a business seeks to raise private debt finance, potential funders (such as banks, private equity and credit funds) may commission a CDD report. Incumbent funders may also request this when considering further funding if the business is underperforming against budgets and expectations, or if there are market developments that may impact a recipient's financial projections and future performance.

Setting the scope

Setting a clear scope that addresses the needs of the commissioner (or the purchaser/lender in the case of V-CDD) is one of the most critical steps in the CDD process. The depth and scope of CDD are influenced by factors such as the size and materiality of the transaction, the commissioner's (or user's) objectives and understanding of the market, and the availability of information (including access to the target entity and its customers and suppliers).

The party commissioning the CDD is responsible for determining the scope of work required, but this is typically done through discussion with the CDD practitioner, who will suggest important areas for consideration.

When supporting the client to define the scope, the CDD practitioner should have a clear understanding of:

- the strategic reasoning behind the client's interest in the target and its long-term desired outcomes;
- the client's key hypotheses for the transaction, as well as their motivations and concerns;
- the deal context, such as the proposed deal structure and transaction perimeter;
- the deal process, including timings and access to information, management and customers;
- the target entity, its markets, customers, geography, maturity, competitors and business model;



- sector dynamics, including specific risks associated with the target entity's sector or business model. Different industries will also often have specific key performance indicators (KPIs) that drive valuations, such as annual recurring revenue (ARR) in a software as a service (SaaS) business;
- the extent of available secondary research;
- the need and ability to undertake primary research; and
- in the case of V-CDD, the needs of a typical purchaser (or lender).

Clearly defining and agreeing the scope helps prevent misinterpretations and expectation gaps. The agreed scope of work should be included in the engagement contract that is signed at the start of the engagement. Throughout the CDD process it is not uncommon for new issues or areas of concern to emerge that the client determines requires further investigation. In such instances, changes to the scope should be documented in an addendum or variation to the engagement contract (see section four for further details on scope of work).

Understanding the limitations of CDD

It is important that commissioners also recognise the limitations of the CDD process. It is best practice for the CDD practitioner to highlight such limitations

and key assumptions within the scope of work (and in the CDD reporting). These will typically include:

- level of access – to the target entity's premises, management, customers, suppliers and other advisers;
- availability of target entity information – the extent of management information and access to a virtual data room (VDR); and
- availability of market information – certain industries, and particularly some niche subsectors, may have data limitations due to the nature of data collection, or the absence of publicly available information and secondary research. In such cases, it is helpful to detail the approach that will be taken to seek to fill such gaps.

In addition, it is important to reinforce that target entity projections and market forecasts are, by their nature, uncertain. For example, the scope wording should note that:

- the realisation of the target entity's projections is dependent on the continuing validity of the assumptions on which they are based and may be materially affected by unforeseen events or changes in market trends, the competitive environment, macro-economic conditions, or geo-political factors; and
- the assumptions will need to be reviewed and revised by the user to reflect any changes in key assumptions.

SECTION

3

ROLES AND RESPONSIBILITIES OF THE CDD PRACTITIONER

It is crucial that the CDD practitioner is objective, free from conflicts of interest and applies professional scepticism. The CDD reporting must also be objective, balanced and based on sufficient evidence-based critique and comment. To deliver this, CDD should be undertaken by persons with professional competence, who have commercial awareness and the appropriate specialist expertise and experience of deals and such work. This includes experience in undertaking both secondary and primary research (eg, interviews with customers, suppliers and industry opinion leaders).

Sector expertise is particularly important to enable the practitioner to effectively appraise a target entity.

If the CDD practitioner does not have the necessary expertise in-house, they may bring in external consultants or subject matter experts to supplement their capabilities.

Applying ICAEW fundamental principles in CDD

As with all engagements, the CDD practitioner should ensure that they comply with the fundamental principles that underpin the ICAEW Code of Ethics. These principles help guide practitioners to deliver objective, high-quality professional work that upholds stakeholder confidence. The following table illustrates the relevance of certain fundamental principles to the CDD proposition.

ICAEW fundamental principles	Examples of relevance to CDD
Integrity Acting with honesty and transparency in all professional dealings.	<ul style="list-style-type: none"> CDD practitioners must ensure that in undertaking primary research and interviewing customers and other third parties they are open and honest in their dealings. They must also fairly represent the position of such third parties in the findings. CDD practitioners must demonstrate professional scepticism by adopting a questioning mind and undertaking a critical assessment of all information relevant to the engagement. The CDD report must not contain anything false or misleading, or omit a matter that would render it misleading. The scope and limitations of the work should be included. This is particularly important where the CDD report will be provided to third parties, such as prospective purchasers in the case of V-CDD or prospective lenders when a buy-side CDD has been commissioned by a purchaser seeking funding for the transaction.
Objectivity Professional or business judgement is not compromised by bias, conflicts of interest or undue influence, or undue reliance on individuals, organisations, technology or other factors.	<ul style="list-style-type: none"> CDD practitioners (including engagement team members) must be able to demonstrate their objectivity and must be free from threats that cannot be adequately safeguarded against, including those arising from conflicts of interest relating to all interested parties (see page 8 for further considerations around conflicts of interest). CDD practitioners must ensure there are appropriate safeguards in place to mitigate against advocacy or familiarity threats – this is particularly important in relation to V-CDD. The CDD report must be balanced and objective with evidence-based findings.
Professional competence and due care Maintaining the professional skill required to ensure quality service.	<ul style="list-style-type: none"> CDD practitioners should possess the requisite experience, commercial acumen and sector knowledge to be able to deliver a high-quality CDD report. It is vital that practitioners stay updated on market and sector trends, apply analytical methodologies and utilise appropriate data analytics and AI tools.
Confidentiality Protecting sensitive client and transaction data.	<ul style="list-style-type: none"> Confidentiality is particularly important in a deal context and when accessing target entity and third-party information. CDD practitioners must have effective policies and procedures for confidentiality and protecting information.
Professional behaviour Adhering to legal and regulatory requirements and avoiding conduct that discredits the profession.	<ul style="list-style-type: none"> CDD practitioners must ensure that they are aware of and comply with all applicable regulations (see page 8). Their conduct should reinforce the credibility of the due diligence process.

Regulatory matters for the CDD practitioner

The CDD practitioner needs to comply with ICAEW's Code of Ethics and other relevant regulatory requirements when accepting and conducting a CDD exercise. Key considerations include, but are not limited to the following.

- **Client acceptance:** CDD practitioners are required to ensure that adequate checks are carried out on all clients before any work is undertaken, including those required by anti-money laundering legislation.
- **Conflicts of interest:** CDD practitioners are often commissioned for their specific sector knowledge and past experience. Nevertheless, to perform a CDD, the CDD practitioner firm and all members of the team must be objective in both fact and appearance. Conflicts must be considered at the outset of an engagement. The engagement must also be monitored throughout to identify any conflicts that may arise. The CDD practitioner should not accept an engagement when conflicts of interest are not considered to be manageable. For manageable conflicts, certain safeguards will need to be put in place, such as separate teams and information barriers. Depending on the circumstances, it may also be necessary to gain consent from the parties involved in the engagement. In a CDD context, with appropriate safeguards and consent, it is possible for separate teams from a practitioner firm to work on both the sell-side and buy-side of a transaction, or indeed to work for multiple prospective purchasers.
- **Auditor independence:** For practitioner firms that carry out both audit and CDD, it is vital that the provision of CDD does not compromise auditor independence. Therefore, at the outset of an engagement, practitioners must consider whether the applicable regulation prohibits the service and, if not, comprehensively assess threats to auditor independence and objectivity in order to determine whether appropriate safeguards can reduce the

threats to an acceptable level such that an objective, reasonably informed third party would consider it appropriate to accept the engagement. Audits are subject to both the Financial Reporting Council's (FRC's) Ethical Standard and the International Ethics Standards Board for Accountants' (IESBA's) Code of Ethics, which provide guidance on prohibited services and safeguards in different circumstances. For example, the FRC's Revised Ethical Standard 2024 (the current version at the date of this guideline) notes that an audit firm is prohibited from undertaking due diligence for public interest entities that it audits.

- **Data protection laws, such as General Data Protection Regulation (GDPR):** Practitioners must ensure that sensitive commercial and personal data is handled securely, with appropriate measures in place for data storage and access control. In most instances, CDD practitioners do not need personally identifiable information to conduct their analysis, so should not handle such data. The target entity should be asked to provide only appropriately sanitised or aggregated information.
- **Securities regulations:** CDD practitioners must comply with financial disclosure requirements and ensure that any material non-public information (MNPI) is handled in accordance with regulatory requirements. As CDDs are typically undertaken on confidential transactions, practitioners must be particularly cognisant of their responsibilities to protect against insider trading, including under the EU/UK Market Abuse Regulation (MAR).
- **Industry-specific regulatory requirements:** In some limited instances, CDD practitioners may need to adhere to sector-specific compliance obligations, such as healthcare industry patient confidentiality standards, pre-employment screening requirements for financial services, or security clearance and vetting requirements in defence.

SECTION

4

CDD SCOPE OF WORK

Considerations for scoping CDD

The scope of work for a CDD exercise can be extensive. What is relevant will depend on the circumstances of the transaction, including the geography, sector, policy and regulatory context, as well as target specifics such as the maturity of the business and any key risks identified (for example, customer concentration, price pressure or competitive differentiation).

On buy-side and other engagements where the party commissioning the work is the beneficiary of the report,

the scope will be tailored to focus on areas that the client determines are most pertinent to their needs. It will also be impacted by access to the target entity and the time available. For V-CDD engagements, there will normally be less restrictive time and access constraints. The scope should reflect what is typically expected by purchasers and may be broader as a result.

Typical scope of work

A fuller scope of work would generally cover the areas in the table on page 10.



Area	Inputs
<p>Business overview</p> <p>This provides an overview of the target entity's services/product offering, key markets, go-to market strategy, business model, historical developments and financial performance, including key sources of profitability, as well as detail on strategic growth plans. This can be used to identify key drivers of performance and key milestones in the development of the business. It may also highlight key customers, suppliers and partners if they are relevant to the target entity.</p> <p>It may involve a more detailed overview of how the target entity's business model is positioned, in the context of the current and future market. This will also consider the scalability and sustainability of the business model. Other aspects such as pricing and marketing strategies can also be covered.</p>	<p>It will typically include analysis of management information, interviews with management and market experts, market research and publicly available information.</p>
<p>Market review</p> <p>This section describes and considers the addressable market for the target entity to provide the context for its performance. This will involve analysing the size and segmentation of that market, as well as historical and projected growth. This can involve an estimate of different addressable market concepts such as total addressable market (TAM), serviceable addressable market (SAM) and serviceable obtainable market (SOM). It may estimate the target entity's share of and share performance in each relevant market segment. A common way to gather these different sources into clear outputs is by building a market model, an internal working tool which brings together the different inputs the CDD practitioner has used to develop a view on market size, growth and segmentation. Key areas that are typically covered include:</p> <ul style="list-style-type: none"> • a clear definition of the market structure, and the relevant market(s)/segment(s) that the target entity operates in; • principal demand drivers and inhibitors that could impact the market (for example, regulatory drivers, macroeconomic drivers, customer/consumer preferences, new products/services, channel developments and technology innovations); • other market dynamics that may impact the market (for example, the influence of key stakeholders, stage of the industry life cycle, demand-supply balance and regulations); and • historical growth rates and future market outlook (over an agreed projected time period). 	<p>Key inputs will generally consist of a mix of primary and secondary research. Common sources include statistical information, published market research, financial accounts, equity or debt analyst research, market and expert interviews, online surveys with customers, consumers or other influencers, and a range of digital datasets (such as online traffic analysis).</p>
<p>Competitive landscape</p> <p>This provides an analysis and summary of the target entity's market positioning, strategy and performance versus its main competitors. It would typically cover areas such as:</p> <ul style="list-style-type: none"> • competitors' performance against industry-relevant KPIs; • an overview of competitor operating models, cost structures and market capacity where these influence competitive performance; • market shares for competitors, as well as the degree of market concentration; • competitive dynamics (such as the costs of customers switching, their loyalty and how intense the competition is); • the target entity's key unique selling point (USP) and areas of differentiation in its operating model, strategic focus, and value proposition; • the defensibility and sustainability of the key USP and differentiators – the strength of the target entity's competitive moat; and • major changes in the market and market structure such as new entrants or industry consolidation. <p>The ultimate objective is to be able to comment on the sustainability of the target entity's market positioning and its outlook.</p>	<p>Key inputs will include management information and interviews, market and expert interviews, analysis of publicly available competitor information (for example, financial statements) and market reports. Depending on the sector, it may include a range of digital datasets (for example, for sentiment analysis across competitors).</p>

Area	Inputs
<p>Customer analysis</p> <p>This is an analysis of the target entity's customer base, such as customer revenue and profit concentration, customer loyalty, retention or churn and how the customer base has evolved over time. It will also include output from customer referencing or surveys, which can be an important element of the CDD, although this will vary depending on the sector, target entity and context of the process. A customer referencing exercise should enable commissioners to gain a better understanding of:</p> <ul style="list-style-type: none"> • why customers engage with the target entity and the strength of its customer relationships; • the target entity's performance across the customers' key purchase criteria; • areas of particular risk or dependency; • the likelihood or intention that the customer will continue to work with the target entity; and • appetite for new products and services, and growth opportunities. 	<p>Access to the target entity's customer information (sometimes on an anonymised basis) is typically requested. In some cases, the target entity may allow access to a number of customers as references. Best practice is for these customers to be selected by the CDD practitioner. However, it may not always be possible for the CDD practitioner to freely select the customer referees. Where this is the case, this limitation should be made clear to the client and any readers of the report. If the target entity has a broad and relatively unconcentrated customer base, then a high-volume online customer survey may be used rather than direct customer referencing.</p>
<p>Pipeline analysis</p> <p>Where relevant this analysis comments on the strength of the target entity's future revenue opportunity pipeline. Analysis typically maps the quality, stage and value of opportunities at different points, and considers likely conversion based on historical performance and revenue targets. This may highlight risks in certain segments or geographies and inform the likelihood of achieving business plan objectives.</p>	<p>It requires high-quality pipeline information (typically from a customer relationship management (CRM) system or pipeline tracker) and may require detailed conversations with the target entity's management. Where possible, prospects and potential customer referencing or prospect surveys (in the case of B2C) may be conducted.</p>
<p>Commentary on opportunities and risks</p> <p>In addition to core work steps, CDD will normally include commentary on some areas outside of the target entity's core business plan. Comments are made on growth opportunities, such as entering new markets, launching new products or expanding customer segments. Commentary will include consideration of how realistic and sustainable these growth opportunities may be. It also identifies key risks for the business, which could include market risks (for example, competitor activity or macroeconomic conditions), regulatory risks, customer risk (for example, reliance on particular types of customer groups) and financial risks.</p>	<p>This commentary is informed by discussions with management, and is anchored in the analysis undertaken within the other areas of the CDD. It will also make use of the CDD practitioner's professional experience and market knowledge but all commentary and recommendations will be based on evidence obtained from the CDD research.</p>
<p>Business plan assessment and achievability of forecast</p> <p>A key objective of the CDD work is to critique and comment on the revenue and margin projections and underlying assumptions prepared by the target entity's management. In some situations this can include upside and downside cases for key assumptions. The critique of business plan assumptions and management forecasts is informed by the full scope of activities performed during the CDD exercise.</p>	<p>Inputs include historical results, the market analysis and other research and analysis undertaken in the areas set out above.</p>

Critique of projections and assumptions

One of the key objectives of CDD is to comment on the main assumptions that drive the business plan's revenue and gross margin projections, taking into account historical performance, as well as market and other commercial research and analysis. As stated in ICAEW's Corporate Finance Faculty guideline on [financial due diligence \(FDD\)](#), this is often done in conjunction with the FDD practitioner.

While the target entity's management team may have prepared a business plan and projections model, the prospective purchaser or client may also often prepare their own buy-side business plan. The CDD findings may be a key input into this, which will then inform the purchaser's valuation of the target entity. In some cases, the client may have strong views on particular assumptions, but it is essential that the CDD practitioner is objective and applies professional scepticism in considering the revenue and margin projections based on available evidence and the CDD work undertaken.



SECTION

5

ACCESS TO INFORMATION AND MANAGEMENT

Access to information and the target entity's management is a fundamental aspect of a CDD exercise. As the target entity's management may need to commit a significant amount of their time, management capacity should be factored into the process timelines from the outset.

The level of access, the type of information shared and how information is provided will vary depending on the circumstances of the deal and the CDD exercise (for example, whether the deal is a competitive auction, involves a listed entity, is buy-side or V-CDD). This is described later in this section.

To start gathering information, the CDD practitioner will usually issue an information request list (IRL) before beginning the engagement, which gives the target entity's management time to prepare this material. The information is then either provided directly or via a data room.

In some situations, the market analysis component of a CDD exercise may be launched solely based on publicly available information and without access to management (for example, if it is being undertaken before a potential purchaser formally approaches a target entity). As noted earlier, it is important that the CDD practitioner makes the commissioner of the CDD exercise aware of the implications when there is no or limited access to the target entity and to clearly state this within the engagement contract and the CDD report.

V-CDD

Vendor-initiated due diligence will normally involve more comprehensive levels of access to both target entity information and management.

- **Access to management:** Full access is typically granted to key executives, with in-depth interviews, site visits and discussions on business strategy, operations and market positioning.
- **Access to information:** All relevant financial and operational data will typically be provided, including detailed management accounts, customer segmentation, market studies and, in some cases, data at an individual transaction level (for example, for direct to consumer (D2C) retail businesses). In some cases, commercially sensitive information (such as customer or pricing information) will be provided to the CDD practitioner, who may agree to present this in the report in an anonymised or aggregated way.

Buy-side CDD

In contrast to V-CDD, access to both information and management is generally more restricted and controlled for a buy-side CDD. However, this can vary significantly at the discretion of the vendors and their financial advisers. If a V-CDD has been provided to the prospective purchaser, and top-up CDD is being undertaken, then access will typically be more limited. The focus will typically be on augmenting the V-CDD and considering more up-to-date information. During the early stages of a buy-side engagement, initial interactions with management often consist of high-level presentations or interviews with senior leadership that focus on clarifying key questions relating to the target entity's business and market positioning.

Transactions involving competitors or specific commercial sensitivity

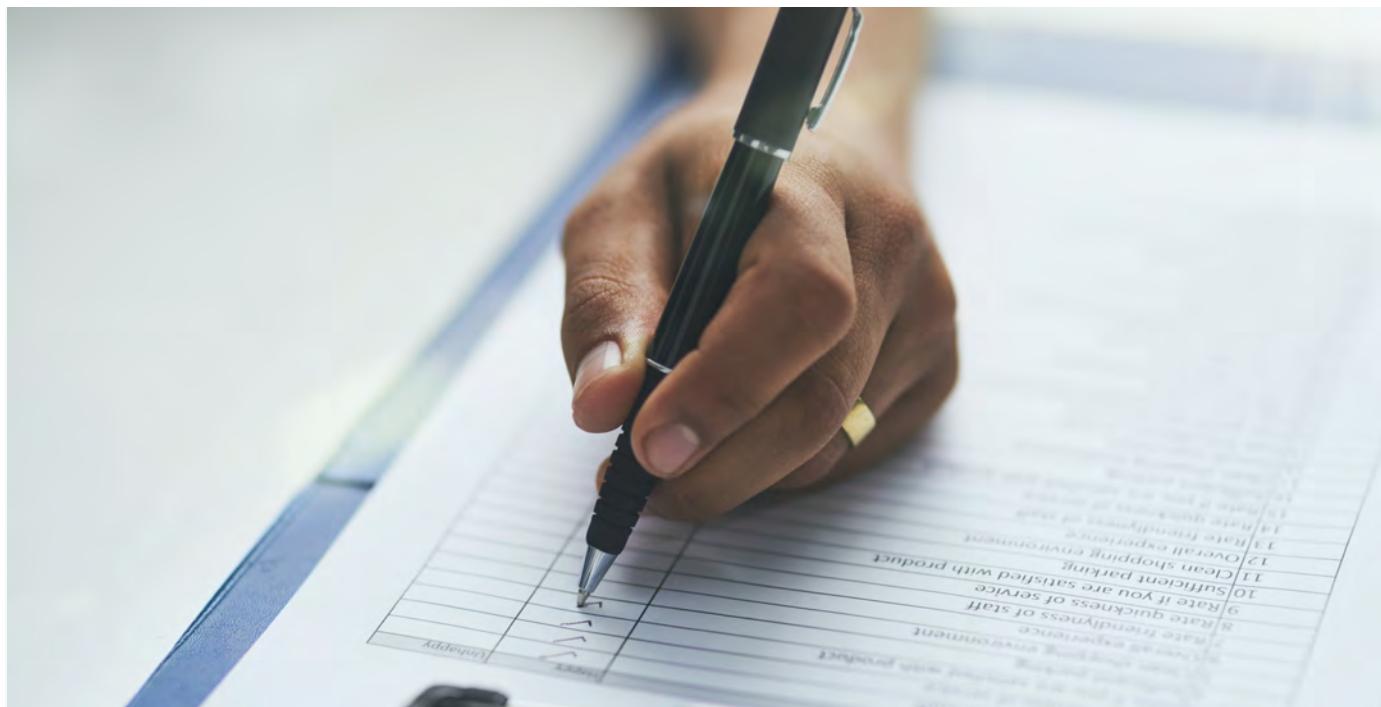
In circumstances where a prospective purchaser is a competitor of the target entity or has other significant commercial relationships with the target entity, the seller or target entity will typically be keen to limit access to confidential strategic information that could be commercially advantageous to the competitor or other party. In some situations, competition law requirements may also preclude sharing certain information. Addressing this may involve:

- strict confidentiality agreements to protect sensitive data;
- clear separation of roles between the prospective purchaser's deal team and any other teams involved in competitive matters at the prospective purchaser; and
- transparency about sensitivity and the establishment of procedures to mitigate the impact on the due diligence process. This may include the use of 'clean teams'.

Clean teams

In cases where commercial sensitivity is a concern, or there are competition authority requirements, the seller may require the use of clean teams. A clean team arrangement in a due diligence context is where it is agreed that the CDD practitioner, and in some cases a specially designated group of individuals at the prospective purchaser, can have access to certain confidential or commercially sensitive information, provided those individuals are separated from the prospective purchaser's main deal team (and such information is not shared with them). The clean teams can consider sensitive information, but the CDD practitioner can only share its findings and such information with the client on an anonymised or aggregated basis.

A clean team agreement between the relevant parties ensures that this process is clearly defined and legally enforceable. It will usually provide that the seller's lawyers review the draft CDD report before it is issued to ensure that confidential and commercially sensitive information is not inadvertently disclosed. The CDD practitioner needs to ensure that the client understands the implications of the clean team agreement, including in relation to CDD reporting. This should be set out in both the engagement contract and in the CDD report.



Auction process: access to information across different rounds

In an auction process where multiple prospective purchasers compete for the same target entity, access to information and management is typically phased across multiple rounds. This structured approach balances the need for transparency (ensuring that prospective purchasers are provided with sufficient information to assess the target entity), with protection of commercially sensitive data. Given that multiple prospective purchasers

are active in auction processes, they are generally prohibited from contacting customers for primary research purposes. If the entity commissioning the buy-side CDD work wants to execute primary research, this will generally be limited to, for example, consumer survey work or interviews with non-customer market experts. The structure of an auction process can vary significantly, but a typical approach is set out below.

ROUND
1

This is typically open to all interested parties. Information provided at this stage is high-level, such as teasers and a confidential information memorandum (CIM) or management presentation. Access to management is generally limited (brief question and answer (Q&A) sessions or high-level management presentations on the business plan), as is the ability to undertake primary research (such as customer interviews). This stage allows prospective purchasers to assess the attractiveness of the business and submit non-binding offers (NBOs).

Before or during round one, initial red flag CDD procedures may be undertaken to highlight potential material issues that could have an impact on the viability of the deal. This could allow the prospective purchaser to walk away before incurring significant deal costs.

ROUND
2

At this stage of the process the field will be limited to a smaller number of prospective purchasers, which have been short-listed based on the NBOs provided. In this round, prospective purchasers will be given access to more detailed data, including granular financial information, customer contracts and VDD reports. In addition, access to management will typically be expanded, with in-depth meetings with key executives (such as the CFO/CEO), management presentations and more focused Q&A sessions. Prospective purchasers can further explore commercial matters and ask questions that arise from the materials provided and their broader research. At the end of this stage, 'best and final' offers are typically submitted.

During round two, greater access to information and management means that more comprehensive CDD can be undertaken, with the prospective purchaser determining the level of scope. Normally access is also offered to the authors of any V-CDD report in "expert sessions".

POST
**ROUND
2**

This usually involves a period of exclusivity, where one or more prospective purchasers gain fuller access to relevant information, including previously restricted sensitive data. Substantial access to management is granted so that final-stage discussions between management and the prospective purchaser(s) can take place. Discussions will relate to operational issues, integration planning and resolving any residual concerns. This is the final stage where price negotiations, terms and the final elements of the sale and purchase agreement (SPA) are discussed, alongside deeper discussions with management on post-deal and integration matters.

Post-round two, with further access being provided, the CDD practitioner may be asked to do any final top-up work required. In some situations, this also involves final stage, confirmatory customer interviews.



SECTION

6

CDD APPROACH AND METHODOLOGY

Key information sources

CDD relies on gathering primary and secondary or desktop research, as well as analysis of a broad range of internal and external datasets. The output provides the qualitative and quantitative evidence to test the key investment hypotheses.

Sources and examples	Key considerations
<p>Desktop research</p> <p>Secondary or desktop research consists of a multitude and incredibly varied sources such as published free or paid-for data compiled by third parties in the form of, for example, trade journals, news articles, competitor financials, announcements and websites. Other sources include regulatory reports, published market research, analyst/broker reports, government statistics, consumer panel or omnibus surveys, retail point of sale data etc.</p> <p>In recent years, CDD practitioners have more commonly integrated alternative data sources into their secondary research methodology to cover gaps in data from traditional sources or to offer additional insights that complement traditional research findings into the target entity or the market dynamics. Examples of alternative sources include social media data (such as customer reviews on Amazon or Trustpilot), anonymised mobile footfall or online traffic data (such as socio-demographic characteristics of people visiting a location or website vs competitors) or credit card transaction data (for example, to understand the target entity's share of wallet (SOW) in a category).</p>	<p>In some cases, secondary or desktop research sources can provide CDD practitioners with a useful starting point to gain a background understanding of a particular sector or to identify key experts to approach for interviews during the primary research. Such sources may provide the quantitative evidence to support or refute some market assumptions. However, desktop research is unlikely to produce sufficiently high-quality insights and granular evidence on its own, given that it can be more general in nature, rather than directly applicable to the specific situation of the target entity. Therefore, primary research, whereby CDD practitioners gather information themselves via interviews, surveys etc, is a key component of a thorough research process.</p>
<p>Primary research</p> <p>In most cases, primary research provides invaluable insight in the CDD process. Steps include, for example:</p> <ul style="list-style-type: none"> • interviews – these may extend to include players across the value chain from suppliers, technology and channel partners, customers (churned, current and prospective), competitors, industry associations, regulators etc. These market participants are often experts in their field and can provide up-to-date facts or perspectives, sector-specific insights and context, shedding light on complex issues that would otherwise be difficult to ascertain via desktop sources. • online surveys – these are a useful primary research tool when a target entity has a large or fragmented customer base, particularly if it is business to consumer (B2C). It enables quick quantifiable data collection on key aspects such as customer satisfaction, key purchase criteria, the competitive landscape, future purchasing intentions and net promoter score (NPS), all of which provide the basis for considering the stickiness of customer relationships and a target entity's ability to maintain its customer base. In some situations, online surveys are also used to capture higher volume, more quantitative insights from, for example, purchasing managers in a business to business (B2B) environment. • other observation tools – such as mystery shopping, site visits or inspections, focus groups, intercept surveys, footfall measurement, platform and tech demos (for tech entities). 	<p>Interviews with top customers, competitors or industry experts can be a particularly insightful primary research tool on more complex questions or on drivers of business success, such as quality of the customer engagement, effectiveness of the go-to-market strategy or scalability of the business. It is vital when undertaking interviews that confidentiality requirements are addressed. For example, the CDD practitioner should agree with the client and the target entity how these interviews will be conducted, such as whether they will be introduced by the target's management or approached directly by the practitioner. To help gain maximum insight from the interviews, CDD practitioners rely on specific interviewing techniques. For example, they develop a structured discussion guide with short open-ended questions, followed by probing questions to gather evidence and explore root causes. In many situations, CDD practitioners will work with expert networks to source market experts for interviews on an anonymous basis.</p>

Sources and examples	Key considerations
<p>Internal target entity data</p> <p>The CDD practitioner also makes extensive use of internal target entity information sources. Broadly speaking these fall into two main but diverse groups:</p> <ul style="list-style-type: none"> • Financial information – this dataset is normally the same information used by the company finance department to assess and report the target entity's financial performance on an ongoing basis. This will include various cuts of the revenue and profit lines, as well as sometimes also cash and/or balance sheet data (depending on target sector and project scope). The purpose of this analysis is to identify trends in historical company performance and what have been the drivers of this. For example, this will involve granular analysis of revenue and profit margins across product groups, geographic markets, customers and customer groups, channels etc. CDD work tends to look at both long-term trends and short-term performance to obtain a best possible understanding of what has driven the target entity's performance. To perform this analysis the CDD will ideally have access to a "data cube" of information from the target entity's finance department – ideally this is the same core dataset used in the financial due diligence process. • Commercial information – this tends to be datasets that are not generated directly from the company finance system but originate from more commercial or operational functions within the business. These types of datasets will vary depending on each situation and scope, but can include customer relationship or sales pipeline and conversion data, customer satisfaction surveys, sales force target and performance data, recruitment pipeline and historical conversion information, one-off analyses of impacts of commercial or marketing activities, supplier and purchasing data, new product development tracking tools etc. The exact nature of these datasets can vary enormously. When making use of these, CDD practitioners need to make a judgement on how reliable and accurate each dataset is and, therefore, how much weight to attribute to them when reaching conclusions. 	<p>The CDD practitioner will normally trigger the gathering of the necessary information by submitting an IRL to the target entity's management team. Once the requested information has been shared and the data analysis has been initiated, the CDD practitioner will use this to help develop the hypotheses (see later in this section). These hypotheses will then normally be discussed and tested in meetings with various members of the target entity's management to obtain further insight into the business performance and its drivers.</p> <p>Internal financial and commercial information requested would normally be shared via a VDR, which is a central digital repository used to manage information access for all parties involved in a transaction process. For example, as part of a V-CDD process a VDR would normally be set up to gather all underlying datasets so these can easily be referenced in reporting output. In due course buyside bidders will normally also be given access to the same data through the VDR.</p>



Hypothesis-driven approach

The hypothesis-driven approach, or iterative issue analysis, is a structured problem-solving method that begins with a clear hypothesis and then systematically seeks to prove or disprove it. In a CDD context, a hypothesis-driven approach typically involves formulating a series of hypothesis statements (often using tools such as an issue tree) that depend on a set of simpler sub-hypotheses or logical statements that can be 'proven' (or otherwise) through analysis and evidence. Generally, the set of hypotheses and underlying conditions would aim to be "mutually exclusive, collectively exhaustive" (MECE) across the key drivers of the target entity's performance.

This approach helps to focus efforts, particularly in identifying and prioritising the analysis needed to prove or disprove the most important hypotheses. This is particularly helpful in transactions with high volumes of data and complex issues, and limited delivery timeframes.

After developing an initial hypothesis (supported by sector knowledge and preparatory research), the CDD practitioner tests this through a research and analysis programme designed to validate or refute each hypothesis. If the analysis does not support the initial hypothesis, the practitioner can adjust it (or move on to the next hypothesis) and carry out refined, additional research and analysis through an iterative process.

Implications of AI and new technology on research approaches

Progress in analytics and AI has given rise to a variety of related tools, including those being developed specifically for a deal environment (see ICAEW's [AI in Corporate Finance hub](#)). For CDD, prevalent current use cases fit within a number of core areas.

Area	How AI and data analytics can help
Information preparation	<ul style="list-style-type: none"> Draft information requests, tailoring CDD-specific requirements that relate to performance, market position, customers and strategy. Generate interview questions to help shape management interviews focused on key business plan assumptions (for example, revenue drivers, market share etc).
Data handling	<ul style="list-style-type: none"> Automatically extract key information and first-stage insights from unstructured data such as interviews, articles, blogs and market reports to search for specific, relevant information. Review data room information through query tools, with the ability to extract and combine inputs from multiple files and identify inconsistencies.
Analysis and trends	<ul style="list-style-type: none"> Identify trends and patterns within very large datasets, for example growth drivers, customer retention rates and sales channel shifts. Undertake financial modelling and analysis to support understanding of revenue evolution, margin trends and forecasting.
Reporting and outputs	<ul style="list-style-type: none"> Generate presentations and visual summaries, or help improve the clarity of messaging or language in reporting (as a drafting assistant). Take and summarise meeting minutes (such as from management interviews, customer calls or internal briefings).

Benefits of using AI

It is important to note the different types of generative AI (GenAI) solutions, and where they are best used. These include:

Category	Description	Examples	Pros and cons
Off-the-shelf AI	Pre-built, general-purpose GenAI tools, accessed via public cloud or application programming interfaces (APIs)	ChatGPT, Gemini, Copilot, Perplexity	Pros: Quick to deploy, easy to use, cheap (or free) Cons: Limited control over data submitted (confidentiality concerns) and model behaviour. Some practitioners therefore do not use certain tools
Embedded/integrated AI	AI capabilities built into enterprise platforms and tools	Microsoft Copilot, Salesforce	Pros: Scalable, user-friendly, integrates with existing workflows Cons: Less flexible/customisable
Private/enterprise AI	Hosted in secure environments, fine-tuned on proprietary or client-specific data	Custom Large Language Model META AI (LLaMA) models, internally developed AI tools	Pros: High security (very effective at managing confidentiality), tailored outputs Cons: Higher cost, more complex to implement

Risks of using AI

It is vital that CDD practitioners understand not only the benefits, but also the risks of using AI and how these can be mitigated through a careful approach.

Category	Description	Mitigations
Risk of leakage of confidential information in AI	Practitioners should be aware that information uploaded into off-the-shelf AI tools, and potentially even offline/walled versions, could be retained or used for future training material, and may subsequently appear in answers for other users.	Practitioners need to ensure that their use of AI adheres to ICAEW's principle of confidentiality and put in place safeguards to avoid the risk that confidential transaction information is divulged to unrelated parties. Some tools will not be suitable for use.
Risk of AI producing inaccurate information	This can be caused by hallucinations (where an AI tool presents inaccurate data), due to, for example, inaccurate, out-of-date or biased data.	As with any datasource, it is the practitioner's responsibility to check and corroborate the accuracy of any AI-assisted research. This should include identifying and interrogating the underlying sources that the AI tool has relied on in the research.
Intellectual property (IP)	AI models may use IP-protected data without obtaining permission or providing adequate acknowledgement, which could violate IP laws.	Using internally generated and owned data would help from a mitigation perspective but could also dilute value.

In summary, it is clear that AI has a significant and growing role to play within CDD. However, it is equally clear that its role will be to augment the work of practitioners, rather than to replace them. AI enables practitioners to perform and accelerate manual tasks, while focusing on the more critical analysis and capturing the implications for the deal.

SECTION

7

CLIENT COMMUNICATION AND REPORTING CDD FINDINGS

Reporting formats

Various reporting formats can be used to communicate CDD findings. The choice will depend on the scope of the due diligence and the requirements of the party commissioning the work. Regular updates and multiple drafts or interim reporting formats may be provided throughout the due diligence process, containing initial analysis and provisional thoughts. However, the final deliverable typically consolidates the findings and final conclusions into a specific written report, which supersedes the earlier interim and provisional reporting provided.

Common reporting formats are written reports and oral presentations.



Oral presentations or briefing notes

- These are often used early in the CDD process to share initial provisional findings or preliminary key issues or concerns. They are sometimes accompanied by slide-based supporting information.



Written reports

Slide-based reports are the most common deliverable for CDD reporting.

- **Red flag report:** In certain circumstances, before agreeing and completing a fuller scope CDD, an initial limited buy-side red flag exercise may be undertaken and reported via a concise red flag report. This focuses only on key issues that prospective purchasers are most concerned about at an early stage. The analysis and output therefore vary depending on client requirements.

- **Detailed CDD report:** These reports generally begin with an executive summary that highlights the most critical findings and issues, such as the evidence supporting or refuting key commercial business plan assumptions. The rest of the report provides detailed supporting analysis across each of the core due diligence areas (see section four for further details). Appendices often contain more granular data and further supplementary information. If the practitioner has been engaged to undertake other types of due diligence, then a single due diligence report covering multiple workstreams may be issued.



SECTION

8

HOW CDD FINDINGS ARE USED

Main uses in a deal context

- **Testing the investment thesis:** CDD provides insight that should help inform prospective purchasers as they test and revise their investment thesis and undertake their valuation. The CDD findings may support or refute the initial thesis, or help inform adjustments, by providing evidence-based findings.
- **Challenging the business plan:** In many situations a key output of a CDD exercise is to critique and challenge the main commercial assumptions that underpin the financial business plan prepared by the target entity or used by the client to support their planned investment. This involves a granular exercise to identify key drivers of the business plan and then challenge the assumptions behind these – as well as any wider implications, such as implied market share development to reach the plan's projections. This exercise will generally result in each of the plan drivers being rated as, red, amber or green (or similar) to provide a view, in light of the work performed, of how achievable they are likely to be.
- **Identification of issues:** One of the most crucial elements of CDD is identifying potential issues or red flags that could significantly affect the transaction. These issues could include commercial risks, market weaknesses, customer exposure, customer dissatisfaction or regulatory concerns. Identifying these risks early allows the prospective purchaser to adjust their transaction strategy, negotiate better terms, or reconsider the transaction altogether. This plays a key role in informing 'go' or 'no-go' decisions.
- **Insight on valuation and negotiation points:** CDD findings can play a significant role in influencing the prospective purchaser's valuation of a target entity. Key insights into the target entity's competitive position, growth prospects and potential risks can impact the prospective purchaser's perception of its value. As such,

issues raised in the CDD may factor into the prospective purchaser's valuation and price negotiation.

- **Raising finance:** Banks or other financial institutions providing private funding for the deal may commission or be given access to the CDD report and use the findings to help assess the sustainability of the target entity's revenue streams and profitability, and to assess the target entity's financial stability and the appropriate level of financing.
- **Third-party uses:** Third parties, such as warranty and indemnity (W&I) insurers, are often given access to CDD reports under no duty/no responsibility (ie, hold harmless) terms and use the report to consider risks in the transaction in the context of providing W&I insurance to either the seller or the purchaser.

Input into other due diligence areas

While CDD focuses on the target entity's revenue and margin projections, and commercial matters, it often intersects with other due diligence workstreams. In some instances, the same due diligence practitioner will be used for multiple different due diligence workstreams. Whether performed by the same or different firms, it is generally preferable for workstreams to be aligned and interact, with duplication of effort therefore avoided.

However, the CDD practitioner would, in these circumstances, not owe a duty of care to the client or other due diligence providers for how the other due diligence providers used the CDD work. They would also not have any responsibility or liability for any other due diligence providers' work or findings, even if they are referred to in the CDD report.

Due diligence workstreams that interact with CDD include:

- **Financial due diligence (FDD):** This considers the financial performance of the target entity, including its earnings, cash flows and assets (see ICAEW's best-practice FDD guideline for further information). There may be a need for interaction between the CDD and FDD workstreams in areas such as historical and projected revenue and margins and customer analysis. Where there is potential for scope overlap (for example, where FDD looks at historical customer churn and CDD at future outlook), it is important to address this early in the process to ensure consistency and efficiency.
- **Operational due diligence (ODD):** This considers the company's operational processes and efficiency. It covers areas such as operating efficiencies, capacity utilisation, supply chain and logistics to consider risks and opportunities in relation to the target entity's business plan and any operational improvement plans. In a carve-out scenario, operational considerations will be an important aspect of assessing the target entity's ability to operate independently and sustainably post-transaction. There can often be important overlaps between ODD and CDD scopes, which will need to be aligned (for example, ODD's assessment of supply chain ramp up or manufacturing capacity will need to be consistent with revenue growth assumptions within the CDD).
- **Technology due diligence (TDD):** This considers the IT systems and whether they are secure, resilient, fit for purpose and scalable for the anticipated growth. The findings of this due diligence and CDD will also need to be consistent (for example, their assessment of the scalability of the target entity will need to align with CDD's assessment of its growth potential).
- **Regulatory due diligence:** This is relevant in some sectors such as financial services, utilities and pharma. It considers the target entity's compliance with industry regulations, potential regulatory risks and the impact of regulatory restrictions on future cash flows or operational flexibility. This due diligence typically goes into much more detail than a FDD or CDD report, which may also touch on these areas. It will be important for the CDD practitioner to be aware of the contents of

the regulatory report and ensure that these are consistent with the CDD findings (for example, do regulatory risks need to be highlighted within the CDD report when considering market outlook).

In most multi-workstream due diligence situations, some degree of co-ordination is expected in relation to the IRL and other requested data (such as management presentation of the business case) to support an efficient process. In addition, where multiple due diligence workstreams are being undertaken concurrently and are likely to have a bearing on each other, regular communication over findings is suggested.

While this is straightforward if workstreams are being delivered by the same provider (for example, CDD, FDD, ODD and TDD), it is not uncommon to have multiple specialist practitioners advising on a single transaction. In this instance, consideration should be given at the start to how and when draft and final findings can be shared between parties, and the legal and contractual mechanisms for doing so (see section nine).

Post-deal strategy and 100-day planning

CDD can play an important role in shaping post-deal strategy and 100-day planning by providing the client with a deep understanding of the target entity's market position, competitive position and customer dynamics. After a transaction is completed, the insights gained from CDD can also help the client identify key areas for value creation. In addition, CDD findings may inform critical decisions such as integrating the target entity, refining business strategies and addressing potential upsides and downside risks.

Most CDD practitioners will also be able to provide value creation advice. For example, this might involve exploring potential opportunities beyond management's existing business plan and helping the client to identify key actions that they could prioritise within their 100-day plan. This is typically focused on high-impact areas that could drive early-stage results, set the tone for the organisational integration and start to build momentum for achieving the desired return on investment.

SECTION

9

OTHER USERS AND THIRD-PARTY ACCESS

Third-party access

CDD practitioners are sometimes asked to consent to certain third parties being given access to buy-side CDD or V-CDD reports. In determining whether it is appropriate to share a CDD report, and on what basis, the practitioner should consider the age of the report, who the client wishes to share the report with, their role and how the third party will use the report.

The practitioner should also consider whether the report contains confidential information that would require approval to share (for example, if the CDD practitioner has signed a non-disclosure agreement (NDA) or hold harmless arrangement with another party to access such information), as well as appropriate and adequate disclaimers. Consent and release are managed by agreeing specific terms and legal provisions with the client and report release terms with the third party.

Forms of report release arrangements

Hold harmless arrangements are a mechanism to manage third-party access to CDD reports. Under these arrangements, the client generally provides authorisation by signing a hold harmless authority letter. The third parties that wish to access the CDD report then sign a hold harmless report release letter and agree, *inter alia*, to confidentiality and use restrictions and that the report preparer has no responsibility or liability to them for the report.

Assumption of responsibility arrangements are used in situations where the CDD report provider has determined:

- that it is appropriate to extend responsibility and liability for the final report to a third party on the basis that the third party accepts the contractual terms; and
- the client has agreed, usually through the inclusion of the mechanism in the engagement contract.

In a buy-side situation, the mechanism is used to provide the final report to co-investors or lenders to the transaction whose interests are aligned with the purchasing party that commissioned the report. This is usually in instances where the scope of work is considered to be broadly consistent with that which those third parties would have required, had they commissioned the work directly. In a V-CDD engagement, the CDD practitioner uses the arrangement to accept responsibility and liability and provide the final V-CDD report to the actual purchaser (and parties connected with the purchaser who are providing debt to fund the transaction).

Typical third-party users

The table on the next page shows typical third-party users of CDD findings. It highlights who they are, why they need access and how the legal provisions (hold harmless and assumption of responsibility) generally apply.

Third party	Role and need for access	Common access arrangements
Prospective purchasers/ lenders in a V-CDD	<ul style="list-style-type: none"> The prospective purchaser/lender obtains the V-CDD report to gain information about the target entity and its strategy to inform its investment or lending decision. 	<ul style="list-style-type: none"> The prospective purchaser/lender accesses the V-CDD report after signing a hold harmless letter (or agreeing to it in a click-through data room). The actual purchaser/lender then signs an assumption of responsibility letter.
Client's advisers	<ul style="list-style-type: none"> Legal and other professional advisers who provide advice to a common client in connection with the transaction/subject matter of the report. 	<ul style="list-style-type: none"> The client is typically permitted to provide access under engagement contract terms of business, provided that the advisers acknowledge that they receive the report on a no responsibility/no liability and confidential basis.
Finance providers	<ul style="list-style-type: none"> Lenders and co-investors making an investment or lending decision to provide private debt or equity in connection with the transaction. The report is used to help inform the decision. 	<ul style="list-style-type: none"> The CDD practitioner typically gives prospective lenders and co-investors access to the report under hold harmless terms and to actual lenders/co-investors participating in the transaction (up to the closing of initial syndication) under assumption of responsibility terms.
W&I insurers	<ul style="list-style-type: none"> For information purposes in connection with their consideration of the transaction and the provision of warranties and indemnity insurance. 	<ul style="list-style-type: none"> They are typically given access by the CDD practitioner on the basis that they accept hold harmless letter terms that the report is confidential, and that the practitioner accepts no responsibility or liability to them.
Regulators	<ul style="list-style-type: none"> Where disclosure is required by law or regulation For information purposes generally to demonstrate that the client has taken advice on a certain matter. 	<ul style="list-style-type: none"> Consent is generally given for the client to provide the report, as long as the regulator is made aware that the report is confidential and that the practitioner accepts no responsibility or liability to them.

CLOSING REMARKS

CDD is a crucial component of the investment appraisal process for organisations considering acquisitions, divestments or raising finance. It helps identify commercial risks and red flags, provides a critique of key assumptions in a target entity's business plan, shapes the target entity's equity story and offers insights to inform the client's valuation.

M&A transactions are becoming increasingly complex, driven by heightened regulatory scrutiny, cross-border challenges, ESG and cybersecurity concerns, increased reliance on intangible assets and evolving stakeholder expectations. As this trend continues, the importance of a robust CDD process will continue to grow. CDD supports prospective purchasers and lenders in understanding the market, the target entity and its position in that market, enabling them to evaluate key risks, new opportunities and the strategic fit of the transaction. In addition, the rapid development of AI technology, and its adoption across the economy, is likely to act as a catalyst for M&A activity, with potential for

increased associated risks. In this environment, CDD is a critical component of any M&A process and an important tool to help drive successful investments and sustainable growth.

The process of executing CDD also keeps evolving. Data analytics and AI technology offer new ways to automate research and analysis tasks and to extract key information from unstructured data and primary research. While these tools cannot replace CDD practitioners, they can support them in executing time-consuming manual tasks at pace, allowing practitioners to focus on critical analysis and generating insights and conclusions. These changes in ways of working will also bring risks, underscoring the importance of integrity, objectivity, professional competence, confidentiality and professional behaviour in CDD engagements. As AI technology inevitably advances, its role in CDD will continue to expand, offering further enhancements to the due diligence process and enabling investors to make better informed investment decisions.

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Yuan is a strategy practitioner with over a decade of experience in market entry, commercial due diligence and strategic options engagements. He leads in particular on investments in energy transition and other infrastructure-like subsectors on behalf of a broad range of public and private sector clients.

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* includes parent companies. Source: ICAEW member data February 2024, Interbrand, Best Global Brands 2023