

What is VDD?

Vendor due diligence (VDD) is a process whereby a company selling itself or a part of its business commissions an independent review of its own business, typically by an accounting firm or other professional services firm, to identify and assess potential risks and opportunities. This information is then shared with potential buyers to facilitate the sale process.

There are several types of vendor due diligence (VDD) that a company may choose to undertake when preparing to sell their business:

1. **Financial due diligence:** This involves a thorough review of the company's financial statements, accounting policies, and financial performance to identify any potential issues or risks that could impact the sale price or attractiveness to buyers.
2. **Commercial due diligence:** This evaluates the company's market position, competitive landscape, customer relationships, and growth prospects to validate the company's commercial viability and future potential.
3. **Tax due diligence:** This assesses the company's tax compliance, tax planning strategies, and potential tax liabilities to identify any tax-related risks or opportunities.
4. **Operational due diligence:** This reviews the company's operational processes, IT systems, supply chain, and human resources to identify any operational risks or inefficiencies that could impact the company's performance.
5. **Legal due diligence:** This assesses the company's legal structure, contracts, intellectual property, and any ongoing or potential legal disputes to identify legal risks and liabilities.

As well as different types of VDD, it can also be done in different ways and in different depths. Outcomes can range from a 'fact book' – a list of pertinent facts about the firm – to detailed reports into every aspect of the company. It is important, therefore, to know what you are paying for and why!

Why is VDD useful?

VDD is expensive and time consuming, but can provide the following benefits in some firms:

1. **Identifies issues early:** VDD allows the seller to identify and address any potential issues or risks before they are discovered by potential buyers. This can help avoid surprises that could derail the sale process or impact the sale price.
2. **Increases transparency:** By providing a comprehensive and objective assessment of the business, VDD increases transparency and builds trust with potential buyers. This can help facilitate a smoother and faster sale process.
3. **Enhances credibility:** VDD reports are typically prepared by reputable third-party firms, which can enhance the credibility of the information provided and give buyers greater confidence in the business.
4. **Strengthens negotiating position:** By having a clear understanding of its own business, including its strengths and weaknesses, the seller can be better prepared to negotiate with potential buyers and justify its asking price.
5. **Saves time and resources:** VDD can help streamline the due diligence process for potential buyers, saving them time and resources. This can be particularly valuable in a competitive bidding process where buyers are looking to move quickly.

The downsides of VDD

I haven't been able to find any evidence that VDD supports higher valuations: It certainly makes life easier for the bank or broker that you're using to sell, and if they're doing the VDD it will certainly increase their profits. I have also seen instances of VDD being pretty disruptive, at a time when senior effort should be entirely focused on revenue generation.

It is also pretty expensive. Legal VDD alone can cost up to £150k for a mid-sized consultancy, financial VDD up to £250k, and commercial VDD up to £200k. Tax VDD will cost somewhere between £25-100k, depending on the complexity of the firm. In total, you can end up paying half a million.

Finally, we might also question, in some cases, if VDD is that useful at all. For a relatively for something that will be out of date in a year and that the buyer will be replicating in any case.

My opinion on the value of VDD

If you have an easy business to sell and your finances aren't complex, then VDD is unlikely to be that useful. However, if you have some significant risks or complex finances then VDD will reassure investors or buyers and speed up the transaction.

I've seen a big range in both the fees for VDD and what is actually done. It's worth breaking down both with anyone you talk to.

VDD can be done in different ways (detailed report vs. fact book). It's important to know what you're paying for. Complete VDD for a £10m revenue boutique is usually less than £300k.

Note: fees for brokerage are usually 2 - 4% of the EV depending on the size of the deal. At the smaller end I'd expect 3 to be a good target and settle for 3.5.