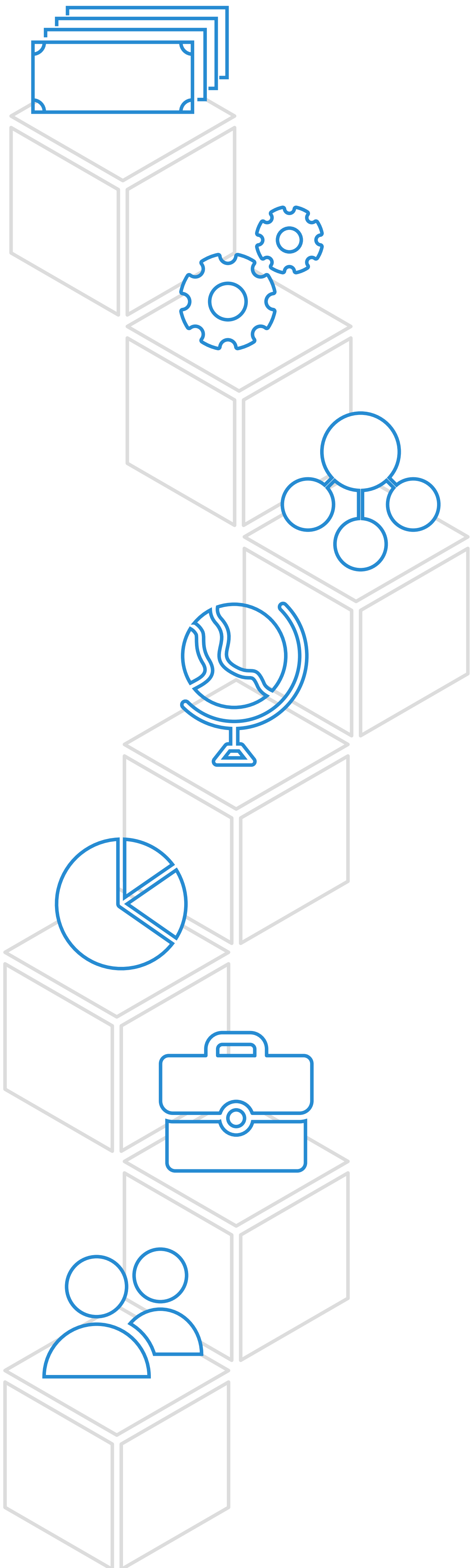
MINTZ GROUP
Clarity in a complex world

The Art & Science of Investor Due Diligence

The high-profile implosions of Theranos, FTX and others in 2022 serve as stark reminders of the need for extensive, dispassionate due diligence by investors—both before committing funds and after the investment has been made. This is particularly true of founder-led entrepreneurial ventures. Unfortunately, in the overheated market of the last few years, even some sophisticated investors let their due diligence standards slip in the rush to get deals done. As the *Financial Times* recently lamented, "doesn't anyone do due diligence anymore?"

Since 1994, Mintz Group has been helping investors from high-net-worth individuals to institutional investors and private equity and venture capital firms—conduct reliable, timely due diligence on companies, management teams and founders around the world. Below, Jill Haberkern sets forth seven best practices for investors to make their due diligence processes as effective and efficient as possible.



1. Know your values—and dealbreakers

The purpose of due diligence is to provide an accurate picture of a potential investment and its management team. But deciding what to do with that picture is up to you. We've had clients who were unfazed by exaggerated education credentials, but then scuttled a deal when our report showed that the target company's CEO had a poor credit history. A target's mediocre record on sustainability may in and of itself have little bearing on your investment thesis but could very well conflict with the values of your organization and its stakeholders. Establishing up front what's important to you also helps the investigations team focus its resources appropriately.

2. Establish controls—and stick to them

There is a natural tension between thorough due diligence and the eagerness to get the deal done. But as recent events remind us, due diligence that is reduced to a box-checking exercise can be worse than no due diligence at all, giving you an illusion of security with no actual reduction in risk. While some aspects of due diligence may be mandated by regulation, for the most part, the due diligence process is a very real test of an organization's ability to maintain its discipline. Incorporate that discipline into the process by establishing controls to ensure that corners aren't cut and potential red flags are addressed.

3. Look beyond the top

Due diligence of entrepreneurial ventures naturally focuses on the CEO—and even more so if she or he is the founder. However, every member of the current management team who will play a key role going forward should be assessed. In each case, the goal should be to piece together a thorough track record that both verifies the experience someone claims in their bio and uncovers any failures they conveniently forgot to mention. Keep in mind that it's possible to conduct different levels of due diligence on different members of the leadership team, depending on their roles and related risks.

4. Keep a global perspective

In today's interconnected, transnational economy, fewer and fewer enterprises and people have purely domestic footprints. However, business, legal and other records are still largely siloed by jurisdiction. When establishing the scope of a due diligence investigation, consider including every country in which the enterprise has had operations or in which the executive has lived, worked or studied.

5. Context is everything

The discovery that an enterprise is facing dozens of lawsuits may appear to be an ominous red flag. But some industries, like consumer products, naturally attract lawsuits, so a high volume of litigation may be nothing out of the ordinary. Similarly, in some countries, companies can't face criminal charges for alleged regulatory violations, so prosecutors go after company officers instead, making it commonplace for an executive to have a history of criminal charges. Experienced investigators can differentiate between routine noise and potential problems.

6. Be prepared to go where the investigation takes you

Investigations begin with a scope that defines who will be investigated and the jurisdictions and timespan covered. But during the course of the investigation, new leads may point in unexpected directions. For example, we once conducted due diligence on a company founder who had an unblemished record - but discovered that the spouse, who was also involved in the business, was indicted for money laundering. Experienced investigators will guide you where they think the investigation should go next—be prepared to adjust accordingly.

7. Consider incorporating subject interviews or questionnaires in the due diligence process

Supplementing investigative research with subject interviews or questionnaires allows investigators to gather important context for any red flags they find, and to learn about issues that are not a matter public record, such as workplace misconduct complaints. Interviews and questionnaires also provide insight into a subject's forthrightness and honesty by allowing a comparison between self disclosure and what investigators uncover.

Mintz Group conducts due diligence investigations for investors, investment banks, law firms and others. Our team of more than 450 investigators in 18 offices around the globe brings a range of interdisciplinary skills and fluency in more than 35 languages to the task of finding clarity in a complex world.

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