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Sharpen M&A with compliance and ethics due diligence

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Companies that are evaluating targets for mergers and acquisitions (M&A) should include compliance and ethics in their due diligence—but these issues are sometimes overlooked in the fast pace of the deal. Compliance and ethics professionals can make a convincing case to their colleagues handling the M&A deal to ensure that diligence on a target company includes legal and regulatory compliance and the company's culture of ethics. Such M&A diligence is even more important in light of compliance challenges due to the coronavirus pandemic.

Getting a seat at the table

Compliance issues matter because, first, they affect the valuation of a company. A valuation can be negatively affected by the uncertainty of pending whistleblower complaints or investigations by government authorities that could lead to monetary penalties. Due diligence enables acquiring companies to spot those issues, conduct a correct valuation, and negotiate that the uncertainty of those proceedings should be borne by the target company. Even more importantly, those complaints or investigations can indicate bad business practices or overstated revenue that may make a deal not worth pursuing.

Next, due diligence can identify misconduct that should be stopped before it results in harm to that company's reputation or profitability, or leads to criminal or civil liability.

In addition, due diligence into the target company's compliance program and identification of any problems before an acquisition leads to a smoother integration of the company after closing the deal. Preacquisition due diligence gives compliance professionals a head start in integrating a target company quickly into the acquiring company's compliance program and remediating any compliance problems that had been identified.

Need another reason for compliance and ethics topics to be covered in due diligence? Enforcement authorities expect it. The Criminal Division of the U.S. Department of Justice (DOJ) states in its June 2020 updated compliance guidance, "A well-designed compliance program should include comprehensive due diligence of any acquisition targets."^[1] Both the DOJ and the U.S. Securities and Exchange Commission view M&A due diligence as demonstrative of a company's commitment to compliance and will take that into account when evaluating a potential enforcement action.^[2] Authorities outside of the United States share the view of the importance of M&A due diligence. The United Kingdom Serious Fraud Office states that mergers and acquisitions is "one type of third party relationship that warrants robust due diligence by an organisation."^[3] And the Organisation for Economic Co-operation and Development encourages companies to consider responsible business conduct risks before entering into an acquisition.^[4]

Finally, companies that identify potentially significant problems when conducting diligence of a target may want

to voluntarily disclose those matters to the relevant authorities. Particularly in the anti-bribery context, companies that discover corruption issues may decide to get ahead of the problem and take advantage of incentives by enforcement authorities like the DOJ that encourage such self-reporting.

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