

Due diligence process - Sweden

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Due diligence

The Purpose

The purpose of carrying out due diligence is to reduce the amount of risk when investing in real estate.

The due diligence process is the checking of a company or a real estate just before the decision to make the deal is to be taken. During due diligence focus is placed on several aspects; the technical, legal, market and the financial. This provides the opportunity to assess the real estate or the company and to check that the information you have received from the broker and/or the seller is correct.

The Process

Almost every time when real estate is changing ownership there is a clause in the contract which says that there is no guarantee against faults. Similarly, you can never claim the seller for faults in the brokers prospectus. This means that the onus is on you as the buyer to perform a proper due diligence process to make sure that the business deal will meet your expectations.

In normal cases due diligence will be done after that the seller and the buyer agree on the price. The buyer will then have a limited time in which to perform their due diligence. That time can vary from one week to a couple of months. If the time period extends to a couple of months, the contract is normally written and the contract stipulates how any faults which may be found during the due diligence process shall be regulated.

The extent of due diligence can be very different from time to time because of the extension of the deal and its form.

A complete due diligence process can be split up in to four sections:

- The real estate - Technical
- The real estate - Contracts
- Conditions, injunctions, environment etc.
- The company

The real estate – Technical

This part is more or less the main part and should always be performed during due diligence for real estate transactions.

Examples of items which should be checked are:

- The real estate's technical status.
- Easements.
- Detailed plans etc.
- Environmental aspects such as PCB and Radon.
- The ventilation control (OVK).
- Systematic fire protection works (SBA)

The real estate – Contracts

Similar to the real estate technical status, its contracts should also be controlled. The major focus should be put on these items:

- The renting contracts must be compared with the invoice list which was used for the calculation.
- Subletting.
- Any possible negotiation agreements with the tenant union.
- Commercial contracts and validity periods etc.
- Any possible discounts.
- Redundant lease.

- Ongoing construction works and repairs.

Permissions, injunctions, environment etc.

During controlling of these areas, focus is put on the real estate and on the businesses which are run in to the real estates.

Examples of this are:

- Environmental audits and reports.
- Evidence, granted requests to the municipality
- Correspondence with the municipality
- Identified or anticipated environmental problems.

The Company

Today, almost every real estate transaction is performed as a company deal. When checking the company there will be many different tasks to be checked..

- The company's owner relationship, income statement and balance sheet should be reviewed and monitored so that the price paid for the shares is correct.
- Any disputes and guarantees that the company is involved in need to be reviewed.
- Agreements that the company has with various parties such as: staff, contractors, Tenant Union/representation and any other companies and organizations.

In our company we normally work with two different types of transactions.

- Company deals
- Real estates deals

Company deals

Currently, company deals are by far the most common form of real estate transactions.

The reason behind this is, that the seller receives a relatively large tax benefit. Nowadays, when doing company deals, the real estate to be sold is most commonly sold into a newly

formed company; this type of activity was not so common earlier.

This method is much easier to control compared with the case of an older company that owned the real estates for a lengthy period of time.

Often, we can settle this in the purchase agreement which means that the due diligence process regarding the company will be reduced in order to correctly calculate the value of the shares based on the company's balance sheet.

If it is a company which has owned and managed the real estate for a longer period of time, the due diligence process is far more complex as all contracts and guarantees with the outside world have to be checked.

Even the calculation of the value of the shares becomes more complex as older companies may often have bank accounts and/or money deposited by tenants etc.

Real estate deals

In transactions made as real estate deals, it is only the real estate and everything that is associated with them that is transferred to the buyer.

This means of course that the due diligence process is relatively easier because the part relating to the company does not have to be dealt with.

Different transactions – different extent

If you always want to be as protected as possible, you should always do a complete due diligence.

The problem is that this would certainly mean that you will miss a number of deals because you need a longer time than other bidders.

A seller easily become nervous, and choose the buyer who can quickly make a clearance.

Similarly, brokers would also have an easy process and often steering the deal to the buyer who is smooth.

Therefore is it important to know what to look for in a due diligence process.

This will save money, and you can move faster while protecting you from risks.

To succeed with this balancing act required certain construction engineering knowledge and experience from real estates. Things you should think about are:

- The year when the building was constructed and/or renovated. By knowing how and with what materials were

used during the different decades, you can set up an idea of the weaknesses that exist.

By knowing this, the possible presence of Radon and PCB with high security determined.

For example, if the construction or renovation year is from 1980 or later can an experienced manager can tell you from outside the building's location and having gone around in the building with a high degree of accuracy of what it costs to run the property.

- What has previously been on the ground? Amplified areas or former industrial sites must always be examined more closely.

- Given incomes must always be coordinated with existing agreements and alert lists .

- The broker. If it is it an odd broker a full due diligence process should always be carried out. The established broker with good reputation often avoids assignments where they know that everything is not right.

I will by this not recommend that you make such a limited due diligence but mostly describe what the focus should be on in situations when time is limited.

Summary

To make as secure transactions as possible while ensuring that you can keep up the tempo required to finish the deal, it is important that all points are checked.

However, a check could consist of, for example, that you know it was not used PCBs in renovations in the 1980s - century and later why measurements need not to be performed.

In this way, the point is controlled without measurements have to be done.

It is therefore important to know what to look for and to achieve this requires experience. A good way to protect yourselves could be to always involve a real estate manager or similar in the due-diligence process.

Such a person is, for example, always up to date on all regulatory requirements, such as *OVK*, *Systematic fire protection (SBA)*, *PCBs* and various city or region-related hazards like *radon*.

