



## DUE DILIGENCE CHECKLIST

*NOTE: Both buyer and seller should perform due diligence on the other party. This checklist is not a complete list, but is intended to cover some of the more common steps other buyers and sellers have taken. Every transaction is unique and the due diligence process must be adapted to the situation by the buyer and seller. Please consult your attorney and CPA for additional information and due diligence steps.*

### INITIAL REVIEW

- ☐ Obtain a written breakdown of the client base showing the number of clients, their states of residence, the number of years each client has been with seller's practice, and how each client selected the seller as their advisor.
- ☐ Obtain a breakdown or production record of the revenue sources to the seller's practice, including types and frequency of revenue generated.
- ☐ Determine the office/business structure (sole practitioner, corporation, limited liability company), including identification of any partners / owners and their ownership interest, employees or other persons licensed to work with seller's client base. Obtain copies of any business plans, descriptions of company, or brochures. Determine who will sign contracts and whether that person / those people has / have authority to perform the proposed transaction.
- ☐ Review Certificate / Articles of Incorporation, Determination, or Organization (or similar documents), including any amendments thereto; By-Laws, Operating Agreements, Partnership Agreements (general or limited) or similar documents, including any amendments thereto; and Minute Books, Consents and Resolutions (since inception) for Shareholders, Members, Board of Directors, and any committees of the foregoing.
- ☐ Review seller's office manual, compliance manual and privacy policy.
- ☐ Determine if seller's reported gross income includes bonuses, awards, or other forms of non-recurring revenues that will not be available to buyer after closing.
- ☐ Determine the amount of broker-dealer override. Similarly, if seller is an investment advisor, determine the annual fees typically charged, the amount of any broker-dealer override on the investment advisory accounts, and whether fees are charged in arrears or advance.
- ☐ Identify any market niches that seller has developed that may prove beneficial to a buyer.
- ☐ Print and confirm that the full-page FP Transitions' Seller's Listing Form represents reasonably accurate data – determine any material changes since the date of listing, and reasons for the changes.
- ☐ Confirm that seller will assist buyer after closing in transitioning the client base to buyer on at least a part-time basis for at least three to six months (larger and more diverse client bases may require additional seller support and transition time).

## CLIENT PROFILE / TRANSFERABILITY ISSUES

- In order to ascertain and address any potential transferability issues, obtain a description of the client base to be acquired, including pertinent factors such as:
  - *Age ranges and demographics;*
  - *Relevant cultural information (e.g., additional holidays, customs to be observed when meeting with clients, etc.); and*
  - *Multi-generational and family related wealth and wealth transfer issues.*
- If this transition involves moving clients from one broker-dealer to another, check with your broker-dealer's policies and personnel regarding portability of client information (Reg S-P).

## LICENSING / REGULATORY INFORMATION

- Obtain a copy of the current Form U-4 for seller (and buyer) and all employees, Form ADV if applicable, along with proof of filing. Confirm filing status and any disciplinary history using FINRA's on-line verification process.
- Review copies of all seller's (and buyer's) securities and business licenses and permits.
- Determine the date of the peer review, or last regulatory audit conducted by state, federal or self-regulatory agencies, and review deficiency letters and any related correspondence. Request information pertaining to resolving any deficiencies.
- Review any correspondence from customers or suppliers relating to complaints or disputes about seller's (and buyer's) practices.
- Obtain copies of each report or other document filed with governmental agencies that have regulatory power over seller (and buyer).
- Obtain a description of all litigation, administrative proceedings, governmental investigations, or inquiries, pending or threatened against, or involving seller (and buyer) or any subsidiary.
- If the other party has a regulatory, legal, compliance, or other issue, then you must investigate such matter(s) and determine if it is prudent to proceed. This is each party's responsibility.

## FINANCIAL AND TAX INFORMATION

- Obtain copies of financial statements of seller (and of buyer) for the past three years, including interim statements for the year to date.
- Obtain copies of federal, state, and local tax returns and reports of seller for the last three years. Sellers should obtain a credit report on the buyer.
- Obtain copies of all documents and correspondence concerning any pending or threatened audit or tax claim against seller or seller's assets.
- Obtain copy of any UCC filings or tax liens from the seller and/or the Secretary of State where the seller's business assets are located.
- Inquire as to whether the Seller has ever had a formal valuation of his/her practice prepared.
- Seller must determine if buyer has the financial ability to purchase the subject practice. This is the seller's responsibility. Seller should obtain satisfactory evidence of ability to pay in writing.

## PURCHASE / NEGOTIATION ISSUES

- Determine general terms of the acquisition, including:
  - *Down payment*
  - *Terms of earn-out arrangement or promissory note*
  - *Seller financing, security/collateral*
  - *Compensation to seller for additional referrals to buyer after closing*
  - *Non-solicitations/non-competition agreements*
  - *Life insurance/disability insurance*
  - *Dispute resolution*
  - *Continuation of seller's license(s)*
  - *Transition period, extent of seller's involvement, duties after closing*
  - *Closing date*

*In times of extreme market turbulence or instability, consider adding language to address volatility.*

## EMPLOYMENT AND LABOR MATTERS

- Obtain a schedule showing the total number of employees, their job classifications, licenses held, average compensation, bonuses, benefits, and location of employment. Review any employment agreements, bonus arrangements, or employee stock-ownership plans.
- Obtain copies of all personnel policy booklets.
- Obtain copies of all collective bargaining and other labor agreements.
- Investigate all pending litigation or administrative matters involving employees, including discrimination charges, grievances, arbitration cases, workers' compensation cases, and similar matters.
- Obtain non-competition/non-solicitation agreements from all licensed and unlicensed staff members.

## PERSONAL PROPERTY (IF APPLICABLE)

- Obtain a list of and inspect all personal property being transferred in the sale (copier, fax machine, phone systems, file cabinets, etc).
- Check UCC filings against all personal property assets.
- Obtain a copy of the original warranties, instructions, and purchase receipts for the assets.
- Obtain copies of any service agreements, and determine ongoing costs for the service and maintenance of the assets.

## AGREEMENTS

□ Obtain copies of the following:

- *All real and personal property leases, including leases for fax machines, copiers, phone systems, DSL lines, etc.*
- *All partnership or joint venture agreements of any partnership in which seller or any subsidiary is a member.*
- *Bylaws and/or operating agreements for any company in which seller, or seller's family member(s), holds an interest.*
- *All agreements pertaining to marketing, including all advertisements, professional dues, etc.*
- *All insurance agreements in force with respect to seller, including general premises liability insurance, errors and omissions insurance, etc.*
- *All material agreements with vendors.*
- *All agreements with officers, directors, and shareholders and their affiliates.*
- *All covenants not to compete, confidentiality agreements, and other restrictive agreements.*

This Due Diligence Checklist is designed to provide general guidance to a wide variety of buyers and sellers of stock or business assets related to a financial services practice and may not be suitable for all users or situations. This document is provided and is to be used with the understanding that the publisher is not engaged in rendering legal, accounting, tax or other professional advice or service. If legal, accounting, tax or other professional advice or assistance is needed, it is the user's responsibility to seek the services of a competent professional.

FP Transitions suggests that buyers and sellers enter into a contingent deal structure in which the majority of the purchase price is paid contingent upon the delivery and retention of client accounts, assets, and cash flows. The use of such a deal structure tends to mitigate poor due diligence or a sudden post closing change in economic conditions affecting the practice. Conversely the larger the cash down payment or the fewer deal payment contingencies, the more thorough and accurate the due diligence process needs to be.

*FP Transitions is the nation's leading provider of equity management, valuation and succession planning services for the financial services industry. Based in Portland, Oregon, FP Transitions operates the largest open market for buying and selling financial service practices in the U.S.*

*Since opening its doors in 1999, FP Transitions has completed more financial service transactions than any investment banker or business-broker in the country. FP Transitions' expertise also includes continuity planning, practice benchmarking, compensation studies, entity formation, mergers and acquisitions, and equity compensation strategies.*



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