

DUE DILIGENCE DIGEST

DUE DILIGENCE DIGEST

April 2011

THE VOICE OF THE DUE DILIGENCE INDUSTRY

Inside This Issue:

Due Diligence is Now a Credentialed Profession from <i>The Aegis Journal</i> , April 2011 by L. Burke Files	2
Dr. Linda S. Spedding, India Law Journal Interview Of The Month India Law Journal, Vol. 4, Issue 1, January-March 2011	4
The Many Faces of Corporate Valuation by Robert A. G. Monks and Alexandra R. Lajoux	9
Profiles in Due Diligence Featured Member Interview: Shaun Hassett	13
ADDP Membership Employment/Contract Opportunities Volunteer & Internship Opportunities	18



Much of what guides company strategy and government policy today is based on flawed premises that must be revised. Progress comes from change, not from a preoccupation with stability that obstructs it.

Michael E. Porter

The Competitive Advantage of Nations



The Association of Due Diligence Professionals

The First Professional Association Dedicated Exclusively to the Due Diligence Industry

Due Diligence is Now a Credentialed Profession
from *The Aegis Journal*, April 2011, by L. Burke Files

The Association of Due Diligence Professionals (ADDP) was founded to provide continuing education, establish professional standards, and provide a forum for professionals to follow the rapidly evolving discipline of Due Diligence. ADDP is the first professional association to recognize due diligence as a unique and separate field, discipline, and industry. They provide the opportunity to earn the equivalent of your Ph.D. in D.D. so one can avoid all of those with a M.S. in B.S.

As odd as this may sound, the ADDP will, in time, fill the same role for Due Diligence Professional, that Association of Certified Anti Money Launderers (ACAMS) has done for money laundering and Association of Certified Fraud Examiners (ACFE) has done for fraud investigations and recovery. ADDP, in its early formation, was driven by a recognition of the need for an independent organization to proactively educate and assist with the understanding of Due Diligence to aid management make informed choices and lower risk by using an earlier version of the discipline, originally termed 'management due diligence'.

ADDP was formally launched in 2009 and is the culmination of 27 years of pioneering efforts to establish the formal discipline of Due Diligence adapted to an increasingly complex world. Based on formal methodology perfected from extensive research, and tested in the real world, the guiding principles of the ADDP are pragmatic, practical, and predictable. With a history dating back to 1984, ADDP brings the qualities of traditional Due Diligence together with a vibrant and contemporary understanding of the issues decision makers face.

Due Diligence is simply the process of pairing representations with facts, and separating truth from fiction - one would think. Yet look at all of the Due Diligence failures around us. Billions vanished, Madoff in prison and now banks, accounting firms, and regulators are being sued to make the investors whole. Where were these "professionals" when it mattered - really where? All claimed to have done "Due Diligence" yet look at the gaping, jaw dropping, failures of their methods. The point I am trying to make here is - they may have been good accountants, bankers and regulators - but they lacked the training in Due Diligence to actually know what questions had to be asked... You see they got good answers to the questions they asked, these supposedly skilled accountants, bankers and regulators just did not know the correct questions to ask.

Modern Due Diligence is a structured, systematic, consistent, and efficient methodology of gathering information to assist in risk assessment and decision management. In assessing the methodologies employed, The Due Diligence Standards from ADDP are used to assign precise, optimum, and practical procedural ratings to the overall process. It really is a science - so as to insure the right questions are asked.

ADDP has Certification Programs bringing the due diligence discipline into the 21st century, to elevate the professionals ability to deliver choice support that is much stronger, dependable, defensible, and with the Due Diligence Index it is possible to rate (score) every part, every function of every organization and thus quantifiable.

The Everyday Due Diligence Tools (EDDTs) bring the level of the full Modern Due Diligence science that may be too much for a given project, the ability, with the EDDTs to apply the science to more of everyday choices. ADDP has the infrastructure to support and continuously improve the discipline and ADDP's Science of Due Diligence™. Local or global, ADDP is providing education, setting standards, certifying professionals, being an advocate, developing tools and research for the profession of Due Diligence.

You will enjoy the training as much as you will the writings and newsletter from the ADDP.

Membership has a two fold benefit, it is about both gaining access to the knowledge base training and certification of the ADDP - but also - ADDP members get access to opportunities, should they come available, for research and consulting assignments as part of a network of ADDP professionals. These opportunities cover a wide range of due diligence requirements in firms ranging from large publicly traded companies to small consultancies. ADDP members can access these private resources to augment the Due Diligence services they provide.

(Disclosure - several professionals within our organization are members and are very much enjoying it.)

L. Burke Files is the Founder of *Financial Examinations & Evaluations, Inc.*, one of the largest independent financial investigation firms, publishers of *The Aegis Journal*, and a **Corporate Member of The Association of Due Diligence Professionals**. Mr. Files is also a **Senior Advisor on the Advisory Board of the Association**.

Mr. Files is a widely recognized expert in the area of financial investigations and due diligence. He has authored numerous articles

and books on the subject, and has presented over 20 seminars on financial investigation subjects. Mr. Files and his firm conduct investigations in the United States, Eastern Europe, Central and South America and China. Before founding FE&E, Inc. Mr. Files was a partner in a regional consulting firm specializing in business, financial and securities consulting. He also served as the Director of Corporate Finance for an investment banking company. Additionally, Mr. Files was a commodities specialist for Oppenheimer/Rouse.

Mr. Files has been quoted in:

- Chief Executive Officer
- The American Southwest Quarterly
- Offshore Journal
- Marketerian and Market Advisors
- John Cooke Fraud Report
- Police and Security News
- The Bodyguard – United Kingdom
- Police Magazine
- European Business
- NPR Market Watch

Mr. Files is the author of the following books and training manuals:

- *Due Diligence for the Financial Professional*. (2nd Edition 2004)
- *Counterfeit Identification*. (1999)
- *Background Investigation – Hire in haste, Repent in Receivership*. (2004)
- *Corporate Financial Investigative Techniques*
- *OPSEC Audit and Review Process*
- *Skip Tracing and its Methodology*
- *Entities for Businesses and Persons*



One of the greatest pains to human nature is the pain of a new idea.

Walter Bagehot

Dr. Linda S. Spedding, India Law Journal Interview Of The Month **India Law Journal**

This article appeared in the India Law Journal, Vol. 4, Issue 1, January-March 2011

This month, India Law Journal's Vikrant Pachnanda spoke to **Dr. Linda S. Spedding, Special International Advisor to the Board of Directors of The Association of Due Diligence Professionals**, about the UK Bribery Act, 2010, which was recently introduced by the UK Ministry of Justice.

Ques: : The UK Bribery Act, 2010 was introduced by the UK Ministry of Justice and will come into effect from April, 2011. Can you explain as to how would this new piece of legislation enable prosecutors to respond more effectively to bribery in the United Kingdom?

Ans: : This new piece of legislation means that there will be, subject to the final guidance, passage and implementation, a specific Act of Parliament in the UK relating to bribery offences that ought to achieve easier prosecutions for the prosecuting or enforcement agency, the Serious Fraud Office (SFO). The recent developments have demonstrated a major shift in that the SFO has shown more willingness to enforce laws already in place, while the new legislation makes it easier to prosecute companies and individuals for corruption. Moreover, the SFO has adopted a new strategy based on a carrot and stick approach whereby companies that self-report their corruption concerns are offered the prospect of a quick investigation and a plea bargain. Those that do not cooperate must face the full force of the law. This approach has led to some criticism from the judiciary and anti-corruption campaigners in view of the potential for plea bargains and willingness to settle defeating the overall objective for the UK to become a

leader in anti-bribery and corruption regimes.

This is an Act that effectively replaces a mixture of other legislation so it is going to be easier to administer. In addition it brings the OECD Convention on Combating Bribery of Foreign Public Officials into the UK law. Since 2002 it has been an offence for UK citizens and businesses to bribe overseas, even if none of the Activity takes place in the UK. Businesses have been sanctioned with multi-million pound fines and individuals have been imprisoned. However, the 2010 legislation raises the platform considerably and must be taken very seriously in terms of business risk management. The legislation covers the practice of offering, promising or giving a bribe, as well as accepting, soliciting or agreeing to receive an illicit payment. Its provisions cover foreign public officials and exposure to prosecution for failed policies, systems and controls – classed as operational risks within banks and financial firms. According to many commentators, the new bribery legislation will make it far easier for companies and senior management to be prosecuted where bribes have been offered, paid or received.

The Act is very short, especially by modern standards, without a lot of complex wording, so it is easy to comprehend. In addition it is deliberately far reaching in its approach, going beyond the jurisdiction of the UK, so a British company that bribes a foreign official in another country or whose local agent does so, can be caught by the Act. It should be noted that as it can extend so far and, in theory at least, cover quite minor offences, the job for the prosecutors will be to concentrate only on serious cases and not trivial ones.

Ques: The test to determine bribery as per this Act is to determine whether the bribe was paid with the intention of gaining business advantage for business in the UK. Do you feel that in the light of this, if socializing with clients could be perceived as an attempt to win business opportunities thereby considering to be an act of bribery?

Ans: As mentioned, we currently do not have the full guidance notes which are key to this legislation and its implementation: moreover we do not know how far the provisions may be watered down to achieve successful passage. As we understand it to date socialising with clients is not in itself likely to be seen as an act of bribery as entertaining a client in an attempt to win business opportunities is not an offence. There has to be an element of impropriety. In essence there are two strands to the offence – first there has to be a financial or other advantage for someone. Secondly, there has to be someone who performs a relevant function or Activity improperly. Nevertheless the payment and the improper Act do not have to be directly linked. To slightly paraphrase the key section of the Act:

-It is an offence where someone offers, promises or gives a financial or other advantage to another person, and he intends the advantage to induce a person to perform improperly a relevant function or Activity, or to reward a person for the improper performance of such a function or Activity.

-It is also an offence where someone offers, promises or gives a financial or other advantage to another person, and he knows or believes that the acceptance of the advantage would itself constitute the improper performance of a relevant function or Activity.

-The person receiving the bribe does not have to be the same person as the person

whose performance is improper.

So taking clients out to dinner is not in itself an offence – especially if the company doing the entertaining has to go through a procurement process to get work from those clients or the real decision makers are not the people in the client company who are being entertained. On the other hand, paying for a senior government official in India to fly to London for three (3) days at the Olympics in the hope of getting a contract is likely to be seen as disproportionate and could be an offence. It is significant that international business culture will also be impacted: the giving of gifts in many places is often regarded as a sign of respect for the recipient. During the Bill's passage through Parliament the Government's representative did note that "to the extent that reasonable hospitality is a normal part of business, we are not seeking to discourage such practices and that the public interest might not be held served by a prosecution unless...the hospitality was excessive or unreasonable". This may be helpful as the Act is not intended to criminalise routine business marketing and evidently the reasonableness of a gift or hospitality will be decided by the discretion of the prosecutor. Meanwhile as regards facilitation payments, whereas it seems unlikely that companies will be prosecuted for small one-off payments to expedite routine administrative functions the Act does not include a minimum threshold and are technically made illegal.

Ques: As per this legislation, businesses in the UK face liability for bribes paid by their employees and business partners, wherever in the world that Activity takes place. Isn't this provision harsh since, the entity may be sued even if it knew nothing about the bribe or had little practical control over the person paying the bribe?

Ans: The objective is to curb bribery anywhere in the world in line with the OECD Convention. And it is probably true to say that bribery is more of a problem – and a way of life – for business outside the UK than within the country. The US Foreign Corrupt Practices Act already has international reach so in that sense this is not new. On the other hand, the new UK legislation is even wider than the US Foreign Corrupt Practices Act, since it has created a zero tolerance regime to ‘facilitation payments’ and because it covers business-to-business transactions as well as business transactions with government or state-owned bodies.

As a further deterrent, the rules also raises the maximum jail term for bribery from seven years to 10 years. A company convicted of ‘negligently failing to prevent bribery’ would face an unlimited fine. Whereas it has been noted that the UK has an unimpressive history in the prosecution of corruption cases - and has received criticism in the past from the United Nations and the US for failing to properly address the issue - the new rules would outstrip even the present US laws. It will be more important to consider appropriate processes that should be put in place to prevent or mitigate prosecutions.

Indeed, there are ways of limiting the risk and there is a potential defence in a case of the sort contemplated by this question: it is a defence to show that a company has ‘adequate procedures in place to prevent bribery on its behalf.’ The Government is due to publish Guidance on this topic before the Act is implemented. It has been suggested that organisations should consider the following precautionary measures:

- draft an anti-bribery policy;
- undertake enquiries into new and existing strategic partnerships;
- conduct a risk management assessment;
- undertake a full due diligence check;

- include the anti-bribery policy on the staff handbook;
- ensure that staff are aware of Actions that are prohibited through training;
- clarify what Actions should be taken to take if anyone comes across bribery;
- make clear what disciplinary Actions will follow in the event of a breach of the anti-bribery policy; and
- integrate whistle blowing procedures.

In practice, this is going to mean that British companies will need to have a Code of Conduct in place that sets out detailed procedures for dealing with third parties designed to avoid dealings which can result in an offence being committed by the company’s directors, employees, consultants or agents.

Undertaking due diligence on prospective agents and representatives as well as steering clear of known bribe-takers in official positions will need to be covered – and the procedures rigorously enforced by the company. It is also going to be important for companies to have adequate safeguards in their contracts with agents and consultants, designed to prohibit any Actions that might cause an offence and including the right to terminate a contract and, perhaps, the right to claim damages if an offence is committed by the agent or consultant.

Ques: Do you think that this Act could help tackle the threat that bribery poses to economic progress and development around the world?

Ans: Yes, though in countries where bribery is endemic, it is going to need official action in those countries as well as imposition of similar legislation on an international basis.

Ques: Do you suggest any further changes that could have been introduced in the Act?

Ans: Not so far although there is concern that it should be less harsh and brought into closer alignment with the US Legislation for various reasons particularly relating to competition and global business practices.

It should be emphasised that, as mentioned above, for some time both international public and private organisations have demonstrated an increased interest in ethical issues involving business – principally in the fields of economic crime and corruption. The OECD and the International Chamber of Commerce (ICC) are two well known organisations that have been working to combat extortion and bribery within the global marketplace. Businesses should be aware that over 140 countries have signed the UN Convention Against Corruption, which criminalises the official solicitation or acceptance of undue advantages in return for official Action or inaction. These initiatives also demonstrate and highlight the gradual agreement on some common, world-wide standards for global business operations, as well as the need to be proactive in dealing with such risks. One way forward, it is submitted, is through the evolution and implementation of sound ethical corporate policies.

Acknowledgement: My thanks to my colleague to Giles Dixon, Solicitor who assisted with these responses.

Dr. Linda S. Spedding is Special International Advisor to the Board of Directors of The Association of Due Diligence Professionals.

Dr. Spedding is one of the few lawyers qualified in three jurisdictions: England and Wales (1975), the United States (1985) and India (1989). Having qualified as one of the youngest female English solicitors, she

trained at Manches and practiced for over ten years at Clifford Turner (now Clifford Chance) and Masons. Dr. Spedding created a niche in international law, where she advised businesses on issues relating to ethical business practice, corporate governance, corporate social responsibility and risk management.

Her first book, “Transnational Legal Practice in the EEC and the USA” is a primary reference source on transnational legal practice. Following her qualification in India, she produced a loose leaf practice service “International Professional Practice” that compared the rights of practice in multiple jurisdictions throughout the world.

As an independent legal adviser in environmental law, she has been involved in a number of donor-financed environmental projects in Asia, notably India. She has advised on corporate social responsibility over many years to enable organizations to integrate these concepts to improve performance within the organizations and achieve a sound reputation. Dr. Spedding has extensive experience in and knowledge of international and comparative developed and developing regulatory regimes. She has assisted with particular regulatory drafting needs, as well as implementation and enforcement aspects in various jurisdictions.

Dr. Spedding has published extensively on environmental law, energy law, due diligence, corporate responsibility and risk management and speaks regularly at conferences and in-house at law firms. She has studied and edited Sanskrit and Vedic origin texts in health, the environment and lifestyle issues and is passionate about the link between traditional positive values and modern living.

Dr. Spedding has dealt with environmental and energy projects that involve advising

appropriate choice of partners, with regard to different environmental regulatory and voluntary frameworks. Having worked in various regions and mixed cultures Dr. Spedding has developed a trans-boundary approach to the provision of her services. She has also assisted in the resolution of issues through alternative dispute resolution outside the usual litigation process and developed a useful understanding and negotiating ability. Over the last two decades she has spent considerable time overseas, particularly in the USA, Europe and India. This experience has enabled her to have a unique understanding in what is involved in international projects.

As a natural extension of her legal practice and legal writing Dr. Spedding became increasingly concerned with issues of risk management and due diligence. Her handbooks have been published and well received internationally, including:

- "Due Diligence Handbook: Corporate Governance, Risk Management and Business Planning", Elsevier October 2008
- "Business Risk Management Handbook: A Sustainable Approach" Elsevier January 2008;
- "Due Diligence and Corporate Governance: A Manual for Business", Elsevier (formerly published by Lexis Nexis October 2004)
- "Due Diligence and Risk Management Newsletter", EMIS Professional Publishing Ltd (1999-2004);

- Contributor to *Due Diligence Practitioners Guide*, Sweet & Maxwell (1999-2007)
- "Trade and Investment in India", Cameron May, 1997
- 2nd Edition, "International Professional Practice", Wiley, 1996
- In preparation *FDI and Globalisation: the Indian Case Study*

She founded *Women in Law* and launched the *Women in Law* service as the pioneering e newsletter for women. *Women in Law* is an international organization of professional women helping other women build meaningful careers and lives.

Over the last 20 years experience, Dr. Spedding has developed beyond compliance and regulatory frameworks to voluntary standards and best practice globally. Her unique qualifications have enhanced an understanding of risk management within organizations having regard to cultural differences within organizations and jurisdictions. She has advised private and public sector organizations on doing business in India, having regard to best practices in terms of environmental, health and safety and regulatory issues, as well as to corporate governance and ethical business practice. She has led missions to India and assisted with MOEF and CII related missions from India to the UK, as well as investment workshops.



Mere unassisted merit advances slowly,
if - what is not very common -
it advances at all

Samuel Johnson



To accomplish great things, we must not
only act but also dream; not only plan but
also believe.

Anatole France

The Many Faces of Corporate Valuation

by Robert A. G. Monks and Alexandra R. Lajoux

This article was excerpted and abridged from *Corporate Valuation: Analyzing Assets, Earnings, Cash Flow, Stock Price, Governance, and Special Situations* by Robert A. G. Monks and Alexandra R. Lajoux (Hoboken, NJ: John Wiley, 2011).

Corporate valuation, an important aspect of due diligence in a merger or acquisition, has many facets. It requires appreciation for what the company owns (assets minus liabilities), for how the company can generate future funds (via earnings and cash flow), and for how the capital marketplace perceives this wealth-creating potential (stock price).

Careful analysis of any one of these aspects of value can improve an investor's sense of a company's worth and hence the possible price ranges for buy, sell, and hold decisions. But valuation need not stop there. These elements can be even more powerful as valuation tools in combination. But how? It starts with the effort to obtain a useful model for valuation.

Building vs. Buying a Model

As in many business decisions, an investor can build or buy a formula for valuation, that is, either create a formula for valuing a company or adopt one already in use. Many investors choose the build route. These do-it-yourself, innovative investors express their valuation idea as a formula and then create software, using open source technology or combining or adapting proprietary technology. The software operationalizes the formula into a proprietary and confidential model.

1. At the simplest level, this can consist of putting a formula into a spreadsheet, but programming extends far beyond this tool.

2. We hope the information contained in this book (combined with other more specialized guides) can help investors build new models or improve the ones they have. The other option is to buy, or at least to adopt, a preexisting formula and model — an approach used by 15 percent of companies.

3. A number of time-tested ones are available for general use, most of them developed in the 1970s during a period of financial innovation and popularized in the 1980s in an active market for corporate control (aka “merger boom”).

We call these programs “hybrid” because they combine a variety of elements; they do not operate strictly in the domain of assets, or earnings, or cash flow, or stock price. We call them “approaches” because they are more than a ratio; they are not just one number compared to another (such as price-to-earnings, Wall Street's most popular metric).

This brief article presents 14 of these existing hybrid approaches to valuation, focusing on the ones that have received some level of attention (based on Web hits) in writings about valuation by investors, managers, regulators, and academics.



The only fence against the world is a thorough knowledge of it.

John Locke

A few of these approaches are associated with developers and/or trademarks or patents, but most are in the public domain, having been developed through common practice and, in some cases, being “obvious” and therefore nonprotectable. Interestingly, whatever their origin, most of these models tend to use the same six key elements as part of their formulas:

1. Some kind of earnings.
2. Some kind of cash flow.
3. Some kind of market value.
4. Some kind of invested capital.
5. Cost of capital.
6. Some measure for return on capital.

Other elements appearing in models include cash on hand, debt, book value of equity, and market value.

Building a Model Within a Model

We are aware that we are offering valuation advice “one company at a time” for investors who have multiple investments. When a stock is part of a portfolio, the individual stock risk-return can be defined as an additional risk-return to the portfolio. The analyst can then compute the covariance of the risk and the return of the stock versus the portfolio. This can be a time-consuming process, which is why many investors use indexes and/or algorithms rather than conducting analysis.

Clearly, any model used to value individual stocks needs to be correlated to a larger model for portfolio management. The skills used in building one valuation model can transfer to the building of the other. The analyst who can value a complex portfolio can apply those same skills to value a complex company.

One of the world’s most successful investors, Warren Buffett, has never laid out a valuation methodology, much less a formula. Rather, he speaks through his actions. Buffett followers report that he favors a relatively small selection of carefully selected, well analyzed stocks; that he eschews exclusive reliance on any single ratio (such as P/E); and that he anticipates (and discounts) future cash flow. Predicting future cash flow is, of course, the ultimate mystery. This article (like the book it draws from) is concerned with developing a workable valuation formula that factors in the future.

Words of Caution

The list of 14 commonly used approaches to corporate valuation listed come with great caution for several reasons:

First, the list is not comprehensive. There are, in fact, countless models. A simple visit to Professor Aswath Damodaran’s Web page for valuation models (at New York University) makes it abundantly clear that there are scores of them.

Second, no sane person would buy a security based on these valuation techniques alone; the techniques provide a reality check on a decision arrived at otherwise.

Third, investors need not take solutions off the shelf; it is better to build one’s own. Indeed, many companies do. (This discussion contains occasional examples of companies using these approaches to judge corporate performance. Note, however, that companies change their approaches over time, as needed, and sometimes abandon off-the-shelf models to create their own.)

Fourteen Approaches

On the other hand, we believe this list of 14 valuation approaches can be very useful to investors or to anyone who wants to analyze the value of a corporation. There are a couple of reasons: If a technique is widely used, then knowing it (and running its numbers) can help an investor predict how others will value a stock — the Keynes beauty contest. Also, these formulas provide content for the algorithms that quantitative traders use.

A corporation's use of a particular model influences its strategic choices, its compensation programs, and its message to the world. So the model becomes a self-fulfilling prophecy. The kind of wealth generated by a corporation focused on one model is different from the kind of wealth created by a corporation using another model. To be sure, everything gets translated into cash; so all the models are after the same goal. Nonetheless, the reason for and the timing of the cash varies according to the model used. And this really does matter. Unless cash is connected to something that is not merely cash — something pertaining to value (a product or service that meets a need in society) — then the cash flow will cease. The more elements models include beyond cash, the more likely they are to predict sustainable value. Here is a simplified list of the approaches, along with the general valuation terms — e.g., “earnings” — for the elements they add, subtract, divide, and/or multiply. (See the following section for the specific terms used by each approach — e.g., “operating surplus” in the cash-value-added approach.)

1. Cash Flow Return on Equity™ (uses cash flow, equity).
2. Cash Flow Return on Investment® (uses assets, cash flow, invested capital).
3. Cash return on gross investment (uses cash flow, invested capital).
4. Cash value added (uses cash flow, invested capital).
5. Discounted free cash flow (uses cash flow, invested capital).
6. Economic Margin Framework
7. Economic Value Added™ (uses earnings, invested capital).
8. Economic value management (earnings, invested capital).
9. Enterprise value (uses liabilities, equity [preferred stock], market cap, cash equivalents).
10. Market Value Added® (uses invested capital, market value).
11. Return on capital employed (uses earnings, assets, liabilities).
12. Return on net assets (uses earnings, assets, invested capital).
13. Shareholder value added (uses liabilities, cash flows).
14. Total shareholder return (uses stock price appreciation plus dividends paid).

Out-of-the-Box vs. Generic, Valuation Models

As already shown, a number of percentages and ratios have risen to the level of an approach to value. An analyst can easily turn the simpler ones into spreadsheets. The proprietary models are more complex and require engaging a vendor. If investors or others don't feel a need to understand the logic of a model, out-of-the-box software enables them to put in numbers and get a result. However, even if investors know the variables, this approach still seems like a black box. Investors should want to know the formula or algorithm that drives the factors.

To Do It Yourself, You Must Take Steps

Investors are constantly valuing aspects of securities, and so they rarely see their process as a series of steps. Yet there are indeed paths to valuation, paths that may vary (even though all roads lead to Rome). For example, Matt Richey, a popular financial blogger, lists these as his steps:

1. Calculate operating free cash flow.
2. Calculate expected growth.
3. Factor in dilution from options.
4. Set a discount rate.
5. Calculate terminal value.
6. Calculate cash per share.
7. Run assumptions through a DCF.
8. Set a range of fair value estimates.
9. Link the DCF value back to the price-to-free-cash-flow (P/FCF) multiple.

This seems to be a good series of steps and constitute a very useful approach to consider, if the only information you have is from financial statements and ticker tapes—often the case in the early stages of due diligence.

Robert A. G. Monks is a pioneering institutional shareholder activist and one of the founders of the field of Corporate Governance.. He founded Institutional Shareholder Services and the LENS Fund, and was chair of the Boston Company. He was a pension administrator in the Department of Labor and was a founding trustee of the Federal Employees Retirement System. Monks is the author or coauthor of a number of books, including 'Corpocracy and The New Global Investors' and with Nell Minow, 'Watching the Watchers', and 'Corporate Governance and Power & Accountability'. He is referred to by *The Economist* and *Fortune* magazines as the leading shareholder activist and governance advocate in the world. He was the recipient of both the Award for Excellence in Corporate Governance from the International Corporate

Governance Network in 2002 and the Award for Outstanding Financial Executive from the Financial Management Association in 2007. Mr. Monks is a graduate of Harvard College, Cambridge University, and Harvard Law School. Mr. Monks also has served in federal government administration as founding Trustee of the Federal Employees' Retirement System and a Director of the United States Synthetic Fuels Corporation both by appointment of President Reagan, and Administrator (office is now Assistant Secretary) of the Office of Pension and Welfare Benefits Administration (Department of Labor) in charge of overseeing the private pension system in the United States.

Alexandra Reed Lajoux, Ph.D., is a Senior Advisor on the Advisory Board of the Association of Due Diligence

Professionals, and is Chief Knowledge Officer at the National Association of Corporate Directors, Washington, DC, a not-for-profit organization dedicated to educating members of corporate boards. A graduate of Bennington College, founded on the "learning by doing" principles of John Dewey, she holds a doctorate in comparative literature from Princeton University and an Executive M.B.A. from Loyola University in Maryland. She has more than 30 years of experience as a senior writer and editor of newsletters, articles, and books on various business topics. She is the author or coauthor of all titles in McGraw-Hill's Art of M&A series, including the recent 2011



One should respect public opinion insofar as is necessary to avoid starvation and keep out of prison; but anything that goes beyond this is voluntary submission to an unnecessary tyranny.

Bertrand Russell

Profiles in Due Diligence

Featured Member Interview: Shaun Hassett

Why did you become a member of The Association of Due Diligence Professionals?

Because it is the only professional organization that is properly focused on the entirety of Due Diligence, and is centered upon expanding both education and proper credentialing in this arena.

Why do you think Due Diligence is so underutilized?

Two reasons: 1. Because many in the compliance, risk management and enterprise management are conditioned to look for easy, check the box answers to more complex problems... and 2. Lack of education/ understanding – as unfortunately, too many practitioners do not understand or perhaps value what true due diligence consists of.

The checklist approach can be misleading, in the sense that many assume a given checklist is “complete”, when in fact they usually are far from complete in most circumstances. The penalty issues involving recent violations of US Sanctions Program exceed hundreds of millions of dollars are always due to failure of due diligence. Examples include :

- Credit Suisse paid \$536m (£329m) to settle a long-running American investigation into payments made to countries on the US's economic sanction list (OFAC).
- Lloyds forfeits \$350m for deliberately disguising origin of funds from Iran and Sudan.
- The largest Bank Secrecy Act penalty ever paid was from Wachovia for \$160 million; related to allowing Mexican exchange houses to launder drug money.

Clearly, there was a failure of proper, thorough Due Diligence processes involved in these events.

What is a little known fact about you or your company?

LUBRINCO Group has been involved in the business of international due diligence, investigative and advisory services for more than 20 years – long before “Due Diligence” was fashionable.

What makes your company unique?

LUBRINCO Group is perhaps one of the best kept secrets in the due diligence and advisory services fields. Almost all of our practice centers around Due Diligence issues – from investigative practice to providing our clients with actionable intelligence – to our AML Compliance services, which centers on helping clients assess their programs and implementing proper procedures, processes and control mechanisms to insure that their compliance program will pass the most ardent regulatory scrutiny.

What keeps you up at night?

How to educate the masses in this arena...

What is your favorite Due Diligence book or article?

As far as books are concerned, *Due Diligence for the Financial Professional*, 2nd Edition, by L Burke Files.

As far as articles are concerned, I have come across several that really focus on importance of implementing proper business processes and the proper implementation of workflows to automate these processes within an organization. Additionally, articles in the Due Diligence Digest are one of the resources I rely upon.

How does your company add value or differentiate itself in the Due Diligence marketplace?

We have a keen understanding of the inner workings within the financial marketplace, and how products and services in the financial sector are gamed and abused by criminals. The principals and practice leaders at LUBRINCO each possess extensive practice experience within various aspects of the financial marketplace, including subject matter expertise in investment banking, offshore financial centers, due diligence services, asset location and recovery and of course in AML/BSA and Sanctions Compliance matters.

What advice would you give to someone who is new to Due Diligence?

Don't settle for less... all too often many practitioners settle for "good enough is good enough" in their Due Diligence efforts and they shortcut themselves and their organizations in the process.

What is the one thing you wish you would have known before getting into the Due Diligence Industry?

How widespread the impact is related to not performing proper Due Diligence and the correlating value that Due Diligence, done correctly, has in building and maintaining high quality business.

Would you like to mention one of your successful Due Diligence projects?

There are a number of projects that come to mind that all have a common theme: In many of our cases, we have been able to uncover information that not only was critical to the final go/no-go business decisions of our clients, but we were able to uncover critical information that other professionals either did not or could not find... in cases that range

from projects centering around art fraud – that led to identifying seemingly unrelated criminal activities, to projects involving financial fraud in areas such as investment fraud, insurance fraud and mortgage fraud, involving a wide spectrum of Due Diligence subjects and issues – and in a number of cases involving identification and recovery of assets back to victims.

What are the most important things one should do to ensure a successful Due Diligence project?

Two of the most basic elements are, plan your work so you can effectively work your plan, and pay attention to not being diverted from working the process. In the due diligence arena, one is always best served to go where the data takes you instead of trying to engage in processes leading to a desired outcome.

How does The Association of Due Diligence Professionals help you drive your organization's strategy?

Participation in the Association allows LUBRINCO to not only stay in the loop with other professionals that understand the value of proper Due Diligence, but also allows us to learn from our peers, and to remain on the cutting edge of issues affecting the Due Diligence profession.



If a Nation expects to be ignorant and free in a state of civilization, it expects what never was and never will be ... if we are to guard against ignorance and remain free, it is the responsibility of every American to be informed.

Thomas Jefferson

Please give us some background on your organization.

The LUBRINCO Group is a boutique firm focused in due diligence and consulting that is focused in the areas of complex financial crimes, including investigation of a wide array of financial frauds, money laundering etc. The group has three core areas of focus – investigation of fraud and other financial crimes and investigations to avoid becoming entangled by those who have “less than desirable” skeletons in their closets, so to speak – location of hidden or missing assets – and helping firms shore up their fraud detection and regulatory compliance efforts to better avoid becoming involved with such activities in the future. This last area can involve helping firms to implement or improve their existing AML/BSA Compliance processes, as well as helping organizations to better identify and protect their intellectual property and critical information assets.

What factors led you to start your firm?

The firm was started out of a need to provide legitimate in-depth Due Diligence to financial service firms and has grown into a boutique international firm.

Which geographies are most interesting to you right now?

Eastern Europe, Russia, and those countries that make up the former Soviet Republic, as well as central and southern Asia, China, and of course our long standing love affair with the Caribbean and Latin America.

How much do you feel the Due Diligence Industry is under-valued today?

Unfortunately, proper Due Diligence processes are tremendously undervalued – either from ignorance of what this process really should entail or from folks who

seemingly fall victim to thinking that “good enough is good enough” when it comes to performing Due Diligence.

What is your ideal Due Diligence project size?

Since no two deals are alike we will entertain projects that may range greatly in size and scope... However, since we only focus on business due diligence matters and cases involving financial fraud (or to avoid involvement with suspect individuals and organizations), or AML/BSA issues, the engagements we are involved in are usually substantial.

What can you tell us about the most promising changes you've seen for the Due Diligence Industry since The Association of Due Diligence Professionals starting helping the industry?

That's easy... ramping up the education and credentials, and the high standards and objectives. People are starting to become more aware of what they don't know.

Here's a simple analogy. You're standing in front of the refrigerator and looking for the special something that I will know when I see it. “I know it's in here... somewhere”

Tell us about your background and your qualifications.

I am a Certified Anti-Money Laundering Specialist (CAMS) and I have been long involved in helping financial organizations in streamlining their AML/BSA/OFAC compliance programs as well as working with firms to incorporate proper risk management and AML/BSA Compliance Issues into their client on boarding and Customer Due Diligence processes.

How does earning the Certified Due Diligence Professional Certification impact your career?

It really sets credentialed due diligence people above professionals that don't have it.

What is the most challenging aspect of your work and how does The Association of Due Diligence Professionals help you tackle that challenge?

There are two most challenging aspects. One is the large amount of false expectations by clients and counsel, because of their lack of understanding of due diligence and to a certain extent the fallout of the 'instant society' we are in. And the second is outreach to the legal community. There are a lot of good lawyers that know their part, the law, but don't know what's required for successful due diligence. The Association shows both of these areas very clearly.

What is your greatest hope for The Association of Due Diligence Professionals going forward?

That the Association becomes recognized by everybody as the educational focal point for due diligence, and the "go-to" place for practitioners to network with other professionals and to be educated.

How are your organization's strategies changing as you incorporate what you are learning from The Association of Due Diligence Professionals?

Our strategies are becoming more keenly focused in our efforts to expand our business and in better targeting specific opportunities where we can be of service.

Shaun M. Hassett is Vice President, Practice Leader and Business Development for The LUBRINCO Group, where he has responsibility for sales and marketing of LUBRINCO's strategic consulting, advisory

and training services. In addition to this role, Shaun also provides consulting and advisory services to clients in the areas of customer/employee due diligence, AML/BSA compliance issues and global sanctions compliance issues.

Prior to LUBRINCO, Mr. Hassett was with Chi-X Global Technology as Vice President, Business Development, Compliance Solutions. Previously, he held multiple roles in both solution sales and strategic alliance management with Accuity (formerly Thomson Financial Publishing), where he was National Account Manager and also served as an AML compliance subject matter expert.

During his career, Mr. Hassett has regularly consulted with regulatory compliance/risk management professionals, operations professionals and legal counsel at leading financial institutions, securities firms, insurance companies, corporations and vendors to the financial community. He has consulted with clients on ways they can improve their customer due diligence and client on-boarding processes, and he has helped improve clients' payment and compliance systems and processes to employ higher "Know Your Customer" standards; and comply with regulations such as the Bank Secrecy Act (BSA), the USA Patriot Act and EU Directives, and those set forth by the U.S. Department of Treasury's Office of Foreign Assets Control (OFAC).

Mr. Hassett is a Senior Advisor on the Advisory Board of the Association of Due Diligence Professionals. He is CAMS Certified, an active member of the Association for Certification of Anti-Money Laundering Specialists, a professional member of the International Association of Financial Crime Investigators and is also on the Advisory Board of the AML Association.

Mr. Hassett has spoken at a number of industry conferences and events on issues related to OFAC/Sanctions Program Compliance, Enhanced Due Diligence, Identification of Politically Exposed Persons (PEPs), Financial Fraudsters and other high-risk entities. His expertise covers a wide range of regulatory compliance standards and practices for the financial services industry, including customer due diligence, employee due diligence, vendor due diligence processes, KYC/CIP business processes and data management, global sanctions program compliance and identification and monitoring of various types of high-risk entities. Mr. Hassett has authored articles on issues including

- Due Diligence and Asset Recovery
- OFAC/Sanctions Program Compliance
- Reducing False Positives in the Interdiction Screening Process
- Due Diligence and Accessing Customer's Information
- Due Diligence and Enhanced Due Diligence: Identification of Politically Exposed Persons (PEPs), Financial Fraudsters and other High-risk Entities
- Performing Due Diligence on Prospective Employees to Reduce Risk

As a Featured Speaker at banking industry conferences, Mr. Hassett has spoken on:

- Reducing False Positives: Bringing Sanity Back to Regulatory Watchlist Screening, Association for Insurance Compliance Professionals (AICP) Conference, Atlanta, GA, October 2008
- AML Update/Best Practices for Insurance, AICP Conference, Atlanta, GA, October 2008
- Reducing False Positives in Regulatory Screening: Update/Best Practices Offshore Alert 6th Annual Due Diligence Conference

& Symposium, Fort Lauderdale, FL, April 2008

- AML Update/Best Practices for Insurance, AICP Conference, Portland, OR, October 2007
- Know Your Customers-KYC Databases: PEPs, Government Black Lists & other KYC tools, Offshore Alert 5th Due Diligence Conference & Symposium, Miami, FL, April 2007
- Know Your Customers-KYC Databases: Customer ID, PEPs & Black List, Offshore Alert 4th Due Diligence Conference & Symposium, Miami, FL, November 2005
- Know Your Customers: Government Watch Lists, Political Figures & other high risk entities; Offshore Alert 3rd Annual Due Diligence Conference, Miami, FL 2004
- OFAC and USA Patriot Act Compliance; ACI Users Group, Vancouver, BC; September 2004
- OFAC & USA PATRIOT Act Compliance; Sungard World 2003, CA



Discovery consists of looking at the same thing as everyone else, and thinking something different.

Albert Szent-Gyorgyi



A man about to speak the truth should keep one foot in the stirrup

Ancient Mongolian Adage

Volunteer Opportunities

There are numerous volunteer opportunities available at the Association. To find out how you can help the Association, please email volunteers@duediligenceassociation.org.

Due Diligence Digest Sponsorship

You can help the Association by sponsoring this newsletter. This is a cost effective way to reach a very targeted audience. Sponsorship can also include guest editorials or featured articles, and we will also include your logo and website. If you are interested please email editor@duediligenceassociation.org.

Editorial Guidelines

We publish a wide variety of articles and other items in the Due Diligence Digest. Here are some guidelines to help you if you are an author or have other items to submit.

Articles can range from 350 to 2,500 words. Topics that help members are the most desired, such as insights you have learned in your due diligence work, helping Members improve their due diligence analysis skills.

Longer articles can be accepted, and we will split the article into two sections and put the larger section on our website.

Book reviews are welcome, especially for books that should be listed on our website as an important reference book for Members. Book reviews typically range from 150 to 750 words. Reviews of new due diligence service tools, software products are also welcome. Interesting interviews are also welcome, such as with due diligence industry experts.

Promotions of commercial products or services are not permitted in articles or departments. If you wish to promote your commercial product or service, you can purchase a newsletter sponsorship section.

We reserve all rights to decline and edit submissions, and which newsletter issue to incorporate submissions.

To submit articles or other items for consideration, please send an email to editor@duediligenceassociation.org.



All rising to a great place is by a winding stair.

Francis Bacon



There's more than one answer to these questions, pointing me in a crooked line.

Indigo Girls



Due Diligence Digest

Publisher	The Association of Due Diligence Professionals
Managing Editor	Georgina K. Lee
Associate Editors	Michael W. Brown Easton Ellsworth
Sponsors	Address inquires to: sponsors@duediligenceassociation.org
Subscriptions	Address inquires to: subscriptions@duediligenceassociation.org
Submissions	Send articles for submission to: editor@duediligenceassociation.org

©2011
The Association of Due
Diligence Professionals

All Rights Reserved

Due Diligence Digest is published 10
times per year by The Association of
Due Diligence Professionals

The Publisher assumes no responsibility for any misprints or claims or actions taken by sponsors. The Publisher reserves the right to refuse any sponsor. No part of this publication may be reproduced in any form or by any means, except as permitted under Section 107 or 108 of the 1976 United States Copyright Act, without the prior written permission of the Publisher.

Parts of this publication may be designed to provide accurate and authoritative information, and are provided with the understanding that the Publisher is not engaged in rendering due diligence professional services. If expert assistance is required, the services of a competent due diligence professional should be sought.

The Association of Due Diligence Professionals
1153 Bergen Parkway Ste M271
Evergreen CO 80439
(303) 430-2888
www.duediligenceassociation.org