

# Product Stewardship Due Diligence

Best Practice for Product & Chemical  
Compliance Due Diligence in Mergers and  
Acquisitions



Wayne Bergin, CPEA  
Principal Consultant  
Product Stewardship, North America  
January 2017  
[www.erm.com](http://www.erm.com)

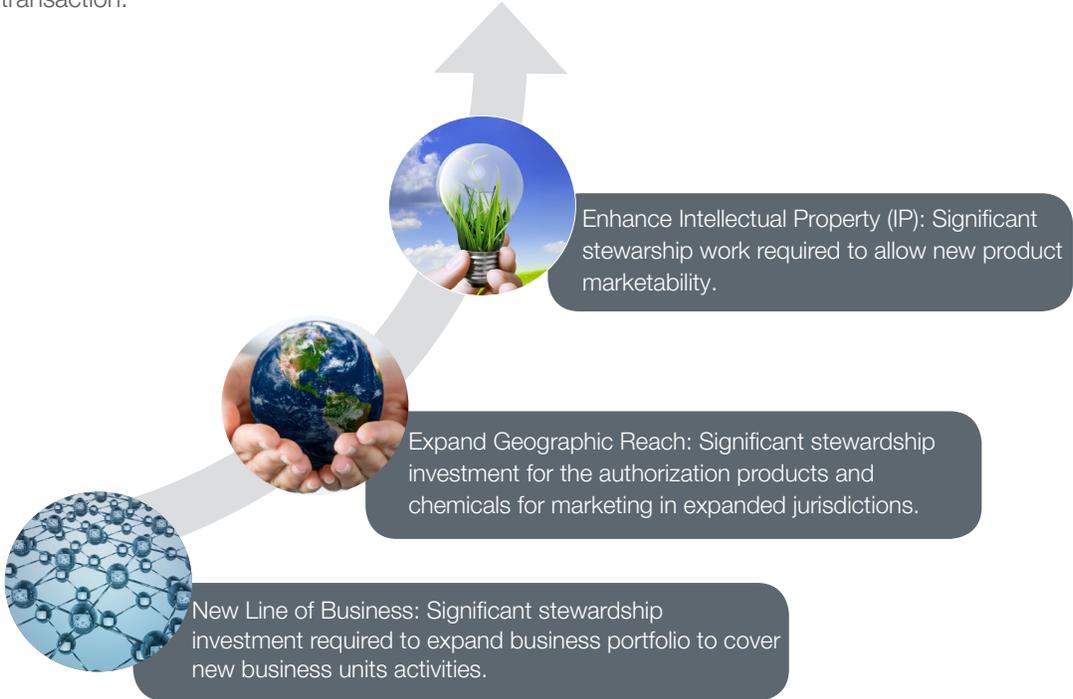
# Best Practice for Product & Chemical Compliance Due Diligence in Mergers and Acquisitions

One of the most important drivers for product stewardship in the face of increasing regulations is to serve the relevant consents and authorizations that allow the sale of products in a global marketplace. However, in the context of mergers and acquisitions (M&A), the stakes are even higher. For example, if a purchaser wants to complete a transaction to acquire a company that sells products in multiple countries worldwide, ensuring the target has the consent to sell those products is critical. After all, what is the value of the business if it cannot sell its products? Herein is the purpose of product stewardship due diligence.

Gaps in product stewardship during M&A can result in lost sales & potentially millions of dollars of fines.

Surveys of C-level executives identify the top reasons for deal-making and include drivers such as: entering new lines of business; expanding geographic reach; and enhancing the intellectual property of a company. These factors can also be product stewardship challenges and often lie at the very heart of the deal's value proposition; they can require considerable due diligence and investment of resources before the value proposition of the deal may be realized.

The intent of effective product stewardship diligence is to look not only at the target company's operations, but also to look ahead and plan for those actions necessary to bring a product to market on Day 1, post-transaction.



So, what does the product stewardship challenge look like in practice in transaction due diligence? Below are two examples of markedly different sized transactions and the common product stewardship issues often encountered when working with our clients on such deals; these examples illustrate that product stewardship challenges can be material in many transactions.

**The small bolt-on** – Often, the driver for such deals can be an innovative new product marketed by the target; alternatively, the driver may be to grow by acquiring a smaller competitor, potentially with a localized sales presence, or indeed to gain access to new market geographies. In this type of transaction, the product stewardship issues most often are gaps in regulatory programs of the target company. These gaps typically result from a lack of resources available to the smaller organization; it is not unusual that these smaller organizations are unprepared for international sales and do not have the tools or expertise to manage their product stewardship obligations. Indeed, a savvy buyer may use gaps identified in diligence as a factor when negotiating the pricing of the deal, or in outlining why the target company needs investments in resources to continue to grow, thereby using its product stewardship expertise as a differentiator in competitive acquisition scenarios. Additional examples of issues include planned synergies for the concentration of operations at a site not being feasible, as permits for use of certain chemicals or raw materials cannot be altered or key substances may soon be restricted in key markets.

**Large multinational spin-off** - At the opposite end of the deal scale is the example of a large multinational company spinning-off a business unit, or a number of business units, as part of a plan to refocus its corporate strategy. These spin-offs often see the business units being acquired by, and integrated into, the operation of a competitor, or indeed run as a separate business altogether. In these cases, it's not unusual for the business units to have sophisticated product stewardship programs in place and be supported by experienced and knowledgeable staff. But even here, the details remain important. Critical product stewardship registrations or approvals may be split over multiple legal entities. Are all the necessary registrations and governmental approvals that are required for the business to operate included in the sale? Unique chemical or product registrations of the spun-off business typically are sold with the deal, but what about registrations needed to trade commodity chemicals, raw materials, or products? Such approvals may be needed for the operation of other seller business units, which are not a part of the transaction. How will these issues be handled? What about product stewardship staff, data, and systems? These often reside at a corporate level and may not be included with the business units to be sold.

Clearly, in a world where product regulatory approvals provide the foundation for product sales and support the underlying cash flow and profitability for a business, product stewardship due diligence is an essential scope item when assessing a potential acquisition.

Product stewardship due diligence may have been viewed in the past as an area with most applicability to the chemical industry, especially for manufacturers of base chemicals; however, with the continued evolution of global regulatory requirements, product stewardship is relevant throughout the supply chain. Every time a raw material, intermediary product, or finished good crosses a border, it is regulated in one way or another and subject to compliance evaluations. As such, in our client work we see the scope for many projects focus not only on chemical style regulations such as European Union (EU) Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH); United States (US) Toxic Substances Control Act (TSCA); or the network of regulations in China that include Ministry of Environmental Protection (MEP) Order 7, but also require consideration of product-specific regulations. These may include regulations on electronics - such as those on waste electrical and electronic equipment (WEEE), batteries, pesticides, biocides, anti-microbials, food contact materials and additives, cosmetics, personal care products, and nanotechnology, amongst others.

When considering these topics and jurisdictions during analysis, ERM experts focus on those regulated topics that can have a material impact on the core business of the target company and that are most important to the sales of our client products.

### What are the obstacles?

Confidentiality is a major obstacle, and one that must be acknowledged to conduct product stewardship due diligence successfully. Product stewardship due diligence may require engagement

over the most important trade secrets of a company – the “secret sauce” that makes the seller’s assets and products attractive for acquisition. There always are data that the seller and target would like to keep confidential during due diligence, particularly where the seller and acquirer are competitors. The challenge is to ensure the seller gives the buyer comfort that the necessary actions have been (or will be) taken to manage product stewardship obligations and challenges, and to do so in a manner that does not undermine confidentiality.

Another foundational issue that makes product stewardship due diligence challenging is that while standards for evaluating financial or environmental health, safety and sustainability (EHS) functions are well established, the processes and procedures for evaluating product stewardship compliance at some companies may be emerging and completely separate from the EHS function. We seldom see a data room folder titled “product stewardship”, and we continue to see product stewardship due diligence overlooked or added at the last minute. Our ongoing iterations with many clients make it clear that it behooves product stewardship and EHS managers to discuss the importance of product stewardship due diligence before the next deal emerges, with the goal of providing input to assign an appropriate value to the target and ultimately secure a budget for necessary product stewardship Post Merger Integration (PMI) activities.

Finally, the sheer variety of products, chemicals, market countries and regulations relevant to a single deal can make for staggering complexity. Within the timeline of a typical deal, one cannot evaluate the compliance of each and every chemical or product in every market country. But a skilled team can identify the most significant risks and opportunities arising from product stewardship.

### How can obstacles be overcome and opportunities identified?

Despite the limitations on due diligence that can result from confidentiality concerns and compliance complexities, a focused review of crucial aspects of product stewardship can typically identify both challenges and opportunities.

A series of high-level diagnostic questions can evoke information about the overall strength of the product stewardship program and the associated information management necessary to provide an indication of compliance. Lines of inquiry into specific products, regulations, and market countries developed in light of the highest volume sales, most valuable product sales, or greatest potential business risk as perceived by the acquirer can provide insights relevant to continuing sales on Day 1 post-transaction. When structured thoughtfully, information gathered at this stage can help the acquiring company determine priorities for action and identify potential process efficiencies after the transaction.

### What about when the deal is done?

There is typically a point in any due diligence progress where the diligence stops being about



identifying the go/no-go issues (e.g., red flags and deal killers), and starts to look at what needs to be done to close the transaction. Product Stewardship PMI is a critical area for work. Due diligence by its very nature is focused on a snapshot of the as is, to-be-acquired company; however, particularly in an acquisition scenario, the product stewardship obligations of the new company can only be understood fully when you look at the structure of the new, post-close company (i.e., the acquirer plus the acquisition target).

The best vignettes for illustrating this point come when our clients consider product stewardship regulations that have a “substance volume” component. EU REACH is a classic example of this type of regulation, but there are many different types of product stewardship regulations globally where a substance’s manufacture and/or importation volumes trigger specific compliance obligations (e.g., US TSCA Low Volume Exemption [LVE], Korea REACH, Malaysia Occupational Safety and Health Classification, Labelling and Safety Data Sheet of Hazardous Chemicals Regulations [known as CLASS], and many others). In an acquisition context, it is clear that a new company can have substantially different obligations from those of either the acquirer or the acquisition target, and these obligations can only be understood based on post-close tonnage in trade. Indeed, ERM and our clients can only manage these compliance obligations effectively if there is a plan to assess these post-close obligations and the necessary tools and resources are in place to manage the integration process in a coherent and structured manner.

Product stewardship PMI is a topic that could be covered by a series of articles of its own; the purpose in raising the topic here is to provide an introduction to the concept as a direct follow-on from diligence.

# Conclusion

Product Stewardship due diligence is essential to realizing the objectives of the deal. By focusing initially on a go/no-go decision you can transition into the PMI planning with confidence. The objectives of this process are to assign the appropriate value to the target and to ensure there is a plan and budget for necessary product stewardship PMI actions to allow sales of product upon closing the deal.

## How to Learn More

Questions or comments? Email the author Wayne Bergin at [wanye.bergin@erm.com](mailto:wanye.bergin@erm.com).



Mr. Bergin is a Principal Consultant at ERM based in New York City. He is a board-certified Professional Environmental Auditor, and has more than 15 years' experience in product stewardship and the environmental compliance industry. Wayne has advised clients on a wide range of transactions and is routinely involved in assessing product stewardship compliance risks and opportunities associated with transactions, post-merger integrations, as well as compliance audits and product stewardship management systems development.

## About ERM

Environmental Resources Management (ERM) is a leading global provider of environmental, health, safety, risk, social consulting services and sustainability related services. We have more than 160 offices in over 40 countries and territories employing more than 4,500 people who work on projects around the world. ERM is committed to providing a service that is consistent, professional and of the highest quality to create value for our clients. We have worked with many of the Global Fortune 500 companies delivering innovative solutions for business and selected government clients helping them understand and manage the sustainability challenges that the world is increasingly facing.