

Due Diligence: Due-Care Examinations in Supplier Relationships and Company Acquisitions

Due diligence denotes the systematic examination of a business partner, company or investment before the conclusion of a contract. In industrial procurement, it covers the assessment of a potential supplier's financial strength, compliance, capacities and sustainability. The aim is to identify risks early and to make negotiation and contracting decisions on a reliable data basis.

Key facts

- Due diligence is a structured examination before contract conclusion, covering commercial viability, legal matters, compliance, quality and sustainability.
- In supplier procurement, it forms the basis for qualification, supplier segmentation and later audits.
- Typical examination areas include financial ratios, certificates, capacities, the supply chain and geopolitical dependencies.
- In practice, a supplier due diligence often takes between a few days and several weeks, depending on the criticality of the supplied scope.
- A contractually agreed right to audit ensures ongoing verification even after the collaboration has begun.
- In M&A transactions, a distinction is made between legal, financial, commercial and operational due diligence.

Definition: due diligence

Due diligence (German: gebotene Sorgfalt, meaning due care) is the systematic investigation and assessment of a contractual partner, target object or supplier before a binding decision. It serves risk minimisation, valuation and the fulfilment of regulatory duties of care.

Distinction from simple supplier selection

The classic supplier enquiry primarily examines price, quality and delivery capability. Due diligence goes beyond this: it assesses financial stability, ownership structure, compliance risks and the resilience of the value chain over a longer period. While selection is often carried out operationally on the basis of enquiry documents, due diligence is an in-depth, frequently project-style examination with defined checklists.

Types of due diligence

Depending on the occasion, several examination fields are distinguished. Particularly relevant in procurement are financial due diligence (financial strength, creditworthiness), legal due diligence (contracts, liability-related issues), operational due diligence (capacities, processes, quality) as well as compliance and ESG checks. In company acquisitions, commercial due diligence (market and

competitive situation) and IT or tax due diligence complete the picture.

Occasions in the industrial environment

Typical occasions are the onboarding of strategic suppliers, a move to a single-source strategy, offshoring or nearshoring, a supplier leveraged buyout or the acquisition of a supplier. Due-care examinations are also customary prior to long-term framework agreements, for example a master service agreement (MSA).

Methods and approach in supplier examination

Execution usually follows a multi-stage process: first a preliminary check based on available data, then an in-depth analysis with questionnaires, document review and, where appropriate, an on-site audit. The scope is determined by the criticality of the supplier.

Preliminary check and data basis

At the outset are supplier master data management and cross-checks with credit agencies, commercial registers, sanctions lists and certificate databases. A meaningful data quality report shows whether master data, certifications and contacts are up to date – otherwise incomplete master data will distort the examination results. In addition, experience from goods receipt is incorporated, such as goods receipt lead time and documented complaints.

Checklist and supplier questionnaire

A structured questionnaire typically covers: legal form and ownership, financial ratios for recent financial years, production capacities, quality management (for example IATF 16949 or ISO 9001), supply chain documentation as well as dangerous goods management where hazardous goods are involved. For electronic components, examining the OEM/ODM model is part of it: who is the actual manufacturer, and who merely trades?

On-site audit and evaluation

For critical parts, an on-site audit follows, assessing manufacturing processes, measurement system capability (for example via gage R&R), batch sizing and control plans. The results feed into a scorecard which, together with the Kraljic matrix, determines how intensively the supplier will be managed in future. Supplier onboarding takes up the examination results and plans maturity levels up to production readiness.

Key KPIs and assessment fields

KPIs make the due-care examination comparable and traceable. They are used both in the initial assessment and in ongoing supplier evaluation.

Financial ratios

Key financial ratios are the equity ratio, liquidity ratios, earnings situation and payment behaviour. The latter is also visible internally in procurement: your own company's on-time payment rate influences how reliably the supplier can plan economically. Payment delays on the buyer's side can tie up the supplier's credit lines and indirectly jeopardise its stability.

Delivery reliability and quality

On-time delivery and the on-time-in-full rate (OTIF) are the most important operational indicators. In addition, first-pass yield, complaint rates, scrap shares and results from safety stock calculation are considered: a supplier whose replenishment lead time fluctuates strongly requires higher safety stocks and therefore working capital.

Risk and sustainability indicators

Country- and supply-chain-specific issues are also assessed: single-source dependencies, transport routes (for example sea freight cost components and their volatility), geopolitical risk of the production site, and evidence of circular economy practices and CO footprint. These fields are gaining weight through supply chain acts and the CSRD.

Risks, controls and contractual safeguards

Due diligence reduces risks but never eliminates them completely. All the more important, therefore, are control mechanisms that remain effective after the contract is concluded.

Typical risk fields

Frequent findings are overstated capacities, flawed cost calculations, hidden subcontractors, insufficient certificates or illiquidity. A classic pitfall is open-book costing: if it is not agreed, price adjustments are difficult to trace later. Implicit price changes are equally critical, for example a unilateral freight surcharge without a contractual basis.

Contractual instruments

A contractually anchored right to audit enables periodic examination of processes, documents and calculations. Price adjustment mechanisms, quality agreements, debt limits and change-of-control clauses ensure that the examined conditions do not shift inappropriately. It is important to design audit rights realistically – deadlines, scope and cost bearing should be clearly regulated.

Ongoing monitoring

Due diligence is not a one-off exercise. Risk-based monitoring combines event monitoring (credit rating changes, sanctions lists, press), regular supplier evaluations based on on-time delivery and sample audits. Buyers document the results in the award record so that decisions remain traceable and defensible – including towards compliance reviews.

Current developments: compliance, ESG and digitalisation

The scope of examination is growing: supply chain acts, sustainability reporting and geopolitical upheavals are extending classical due diligence with new mandatory and examination fields.

Supply chain acts and ESG

Companies in Germany must systematically analyse human rights and environmental risks in their own supply chain and derive measures from them. The supplier declarations required for this, covering codes of conduct, origin and working conditions, are an integral part of modern due diligence. Legal bases and thresholds change – implementation should always be reviewed legally on a case-by-case basis.

Geopolitics and supply chain diversification

Trade conflicts, export controls and raw material dependencies make geopolitical risk a fixed examination criterion. Many procurement organisations now also assess suppliers on how well they support multi-sourcing strategies, regionalisation or nearshoring. The results feed into supplier segmentation and contingency plans.

Digitalisation of the examination

Platform-based supplier profiles, automated sanctions list screenings and AI-supported risk signals significantly accelerate the preliminary check. Nevertheless, digitalisation does not replace the in-depth manual examination for critical suppliers – it shifts it to the points where human expertise is genuinely needed.

Due diligence in M&A and demand-side selection in tenders

Besides supplier examination, due diligence plays a central role in company acquisitions and in preparing structured procurement procedures.

Due diligence in the M&A process

When acquiring a supplier, buyers typically examine financial position, contracts, personnel, environmental liabilities, IP and IT. Important for buyers: existing supply contracts and their transferability, dependencies on key individuals and hidden liabilities. The findings feed into purchase price reductions, warranties or conditions precedent.

Examination in the context of tenders

Even before an e-auction preparation or a structured RFQ, a minimum due diligence makes sense: only bid-capable, stable providers should be admitted. This includes a credit check, capacity confirmation and clarifying whether quoted prices are comparable including all price- and terms-maintenance-relevant components (freight, packaging, tooling).

Typical metrics

Supplier equity ratio: > 20 %

Common benchmark for stable mid-sized companies; industry-dependent.

On-time payment rate (own payment behaviour): > 98 %

Influencing factor for supplier liquidity and delivery reliability.

Supplier on-time delivery: > 95 %

Key indicator in ongoing supplier evaluation.

Audit penetration (audited critical suppliers): > 90 %

Proportion of A-suppliers audited within an audit cycle, typically 2–3 years.

Practical example

A mid-sized mechanical engineering company wanted to qualify a new supplier for complex welded assemblies after the incumbent single-source supplier became a delivery risk. Before the framework agreement, procurement carried out a staged due diligence.

- Preliminary check using a credit report, sanctions list screening and cross-check of supplier master

data

- Two-week on-site audit focusing on welding processes, gage R&R of measuring equipment and batch sizing
- Contractual anchoring of a right to audit, open-book costing and clear rules on freight surcharges
- Inclusion of the supplier in supplier segmentation as a strategic partner with quarterly on-time delivery reporting

Conclusion

In industrial procurement, due diligence is more than a formality: it protects against financial losses, quality problems and compliance breaches and creates the data basis for sustainable procurement decisions. What matters is a risk-based scope – not every supplier needs a full audit, but every strategic partner needs a reliable examination. Those who document examination results, secure them contractually and monitor them continuously turn due diligence from a one-off check into an ongoing risk management tool. This reduces not only default risks but also hidden costs from safety stocks and replacement sourcing.

Frequently asked questions

What does due diligence mean in simple terms?

Due diligence means “due care” and refers to the careful examination of a business partner before entering into a collaboration. In procurement this means: before concluding contracts, you examine a supplier's financial strength, qualifications, compliance and capacities. The aim is to identify risks early.

What types of due diligence are there?

The usual distinction is between financial, legal, commercial, operational and tax due diligence. In the supplier context, compliance, ESG and quality assessments are added. Depending on the occasion – supplier qualification or a company acquisition – scope and focus vary considerably.

How does a supplier due diligence proceed?

Typically in three stages: first a preliminary check using credit agencies, sanctions lists and master data, then a structured questionnaire covering finance, quality and compliance, and finally, where appropriate, an on-site audit. The results feed into an evaluation and form the basis for contract negotiations and supplier onboarding.

Who is responsible for due diligence?

In procurement, the responsible category manager or supplier qualifier usually owns the process. Legal, quality management, controlling and compliance provide specialist input. In M&A transactions, external advisors often coordinate the examination, but responsibility for content remains with the client.

How long does a due diligence take?

A supplier preliminary check can be done within a few days; an in-depth package with an audit often takes two to six weeks in practice. In M&A processes, four to twelve weeks are typical, depending on transaction size and data availability. Good preparation with clear examination checklists significantly shortens the process.

What is the difference between due diligence and an audit?

Due diligence takes place before the contract is concluded and assesses a partner's overall suitability. An audit is a one-off or periodic examination of individual areas, such as quality management, and can also take place during the ongoing collaboration. In practice, the two tools complement each other.