

Dangerous grounds

Mark T. Townsend examines the importance of business intelligence and due diligence when assessing risk in UK and overseas markets.

What would happen if you discovered that the prospective partner in a new joint venture agreement had links to corruption or criminal activity? Expressing shock and outrage are no longer acceptable reactions in an increasingly frenzied commercial environment.

In 2003, UK exports to China rose by 29%, according to the Office for National Statistics. When these figures are viewed in conjunction with China's astonishing 9.1% annual rate of GDP growth in 2003, they will undoubtedly presage greater trade and investment with one of the world's fastest growing economies.

However, there are significant risks for companies and practitioners new to international commerce. Often, corners will be cut in the pursuit of profits, setting the scene for future casualties in many commercial relationships with potential losses in investment and reputation. Damage to reputation frequently ranks as one of the most critical risks faced by companies and practitioners alike.

Small steps

Before entering any new market it is important to carry out an evaluation of the risk using proven business intelligence methods. In countries and regions such as China, the Middle East and Russia, standards of corporate governance, transparency and intellectual property protection are evolving but are often lower than in the UK. In key growth areas such as financial services and telecoms – where the UK has global expertise – it is important to assess what protection will be granted in the local marketplace.

It is equally important to carry out an integrity check on the proposed business partner and examine their relationship with the local business environment. Carefully consider the accuracy of any claims relating to reputation, business performance, and influential

links, alongside a review of company culture with an analysis of the ethics of key executives. Thereafter, inspect financial statements with an emphasis on the nondisclosure of any pertinent information and identify any 'red flags', i.e. unusual payment patterns or financial arrangements. As has been frequently identified in Russia and the CIS, this research could mean – in the extreme – uncovering links to organised crime, corruption and money laundering.

This analysis matters at home too. UK companies are under a tightening regulatory environment where the drive to improve corporate governance appears almost omnipresent. Aside from the UK's current stringent money laundering laws, if the Financial Reporting Council gets its way, directors will soon have to certify the effectiveness of internal controls. In practice areas such as the increasingly cross-border nature of M&A and forensic accounting, expanded due diligence will loom large. The recent surge in cases of directors' criminality is well-documented, as is the struggling success rate of prosecution by the Serious Fraud Office. Getting a handle on these issues at the start may not eliminate them from occurring, but will help to reduce the possibility significantly.

Plans are nothing, planning is everything

The necessity to mitigate risk is often overlooked at the early stages of new market development, particularly when competitive pressures dictate the necessity for quick decisions. Instituting a business intelligence strategy and incorporating this into the planning process will ensure authoritative information is obtained about a market and an intended partner. This will not only prevent expensive commercial errors, but will also eliminate the chances of being associated with a business that has a sideline in suitcases containing generous traveling expenses.


Instituting a business intelligence strategy and incorporating this into the planning process will ensure authoritative information is obtained about a market and an intended partner.

There is no systemic template that fits all markets and there is risk in all business transactions. Different markets will require different judgments and it is important to take into account divergence in culture, both business and social, when planning due diligence in a market or partner strategy.

The consequences of not fully assessing risk are far-reaching and could have legal outcomes, both civil and criminal. At lesser levels it may simply mean claims made by management are inflated or even invented, with the result that revenue targets



Mark T. Townsend

will not be met. Due diligence now has a wider remit than ever before and demands a particular skill set to ensure compliance with regulatory requirements. Consider what internal resources are available to fulfill this analysis, as there are complex issues to be dealt with. 

Mark T. Townsend is the founder of Synthesis Management Consultants.
Tel: 01202 534751
info@synthesismc.co.uk

SHACK SIEGEL KATZ & FLAHERTY P.C.

COUNSELORS – AT – LAW

530 FIFTH AVENUE
NEW YORK, NY 10036

TELEPHONE: (212) 782-0700

FACSIMILE: (212) 730-1964

Our primary focus is to provide clients with a breadth of business oriented legal advice, emphasizing sophisticated corporate transactional representation and practical corporate counseling for both publicly-owned and privately-held clients. Areas in which we have extensive experience include public and private financings, securities transactions, mergers and acquisitions, business start-ups, intellectual property, shareholder arrangements, product licensing, manufacturing and distribution arrangements, joint ventures, real estate, business counselling and employment matters.

Our goal is to provide our clients with the highest quality legal services in the most efficient, effective and economic manner. We specialize in our clients' businesses which are varied and include development and manufacturing of videogames; manufacturing of food equipment; gaming machines; medical equipment; industrial filtration fabrics and baking ingredients; publishing (magazines, books and music); retail clothing chains; restaurants; hotels; and insurance brokerage. We believe that excellence of service goes hand in hand with experience and trusted familiarity with a client's business.