

## **Penny Wise Pound Foolish**

Nearly 80% of UK CEOs and FDs believe their business is at risk during this recession yet few realise that this risk includes potential litigation following cost cutting measures

Nearly 80% of UK CEOs and FDs believe that the recession has increased the number of risks that their businesses face and over 50% of them have sought to reduce costs or share financial risk since the beginning of 2008. However 75% of these businesses do not understand that cost cutting exercises such as outsourcing have actually increased their risk of being drawn into litigation which can be both difficult and expensive.

In a survey commissioned by the Forensic Accounting Team at BDO LLP to look closer at the likely causes of the increase in litigation associated with a recession, it was also found that half of UK companies have sought to reduce their costs by increasing their use of subcontractors and freelancers, by outsourcing activities such as support services or relocating facilities offshore and granting product licenses.

Almost half of these companies believe that performance and conduct of these subcontractors, franchisees or sales agents could in fact damage the company's market reputation or brand resulting from poor performance by subcontractors; reliance on outsourcers interrupting the quality or continuity of supply or commercial harm arising from damage to intellectual property or relationships with key customers. And these are all issues that are frequently the basis for disputes that can end in damaging and expensive litigation.

Three quarters of all businesses surveyed have sought to cut costs by reducing headcount, either through natural attrition – by not replacing roles – or through formal redundancy programmes.

Mike Mason, Director of Forensic Accounting at the Southampton office of BDO LLP says:

Few businesses have managed to come through the challenging economic environment of the last 18 months entirely unscathed. The speed and extent of the recession has forced many to make tough choices and to find innovative ways to cut costs and manage their business.

It is evident from some of the disputes that we have been instructed upon that businesses often expose themselves to enormous commercial risks which can result in disputes and litigation.

Measures, such as redundancies, outsourcing support services, relocating production facilities offshore or joint venture arrangements have the potential to deliver significant cost savings but measures that focus purely on the cheapest solution can sometime have unwelcome side effects on service delivery and profits. It can be extremely difficult for businesses to extricate themselves from such arrangements and the claims and counter claims require careful quantification .

In times of recession businesses run an increased risk of becoming embroiled in a wide range of disputes as contractual non performance and onerous contracts have a more significant impact on profits and the diverging interests of commercial partners and shareholders come into sharper focus.

Mason adds:

The depth and speed of the recession did not herald the anticipated upturn in disputes as parties were mindful of the cost and operational disruption that often accompanies such disputes. With recovery on the horizon we are beginning to see an increase in claims as contractual arrangements that are not delivering in line with expectations are coming under intense and critical scrutiny as

businesses take stock of the merits of bringing a claim.

Many of the disputes that we are being instructed upon arise from the need to obtain independent accountancy advice where non core businesses have been sold and one of the parties has sought to renegotiate the consideration via a net asset clause .

– Ends –

About the Research:

The full findings of the survey and corresponding analysis can be found in the research report published by BDO on 14th December 2009 entitled Penny Wise, Pound Foolish .

BDO commissioned ICM Research to carry out a survey of CEOs and Finance Directors at 201 companies of varying size across the UK in September 2009.

For further editorial information about Logical Creative Marketing please contact Zoe Mitchell on 0845 345 6969 or email [zoe@lcm.co.uk](mailto:zoe@lcm.co.uk)

Notes to editors:

BDO LLP operates across the UK with some 3,000 partners and staff. BDO LLP is a UK limited liability partnership and a UK Member Firm of BDO International. BDO – Belfast, a separate partnership, operates under a licence agreement. BDO International is a world-wide network of public accounting firms, called BDO Member Firms. Each BDO Member Firm is an independent legal entity world-wide and no BDO Member Firm is responsible for the acts and omissions of another member.

The network is coordinated by BDO Global Coordination B.V., incorporated in the Netherlands with its statutory seat in Eindhoven (trade register registration number 33205251) and with an office at Boulevard de la Woluwe 60, 1200 Brussels, Belgium, where the International Executive Office is located.

The combined fee income of all the BDO Member Firms was \$5.14 billion in 2008. The global network has 1,095 offices in 110 countries and more than 44,000 partners and staff provide business advisory services throughout the world.

BDO LLP and BDO – Belfast are both separately authorised and regulated by the Financial Services Authority to conduct investment business.

BDO is the brand name for the BDO International network and for each of the BDO Member Firms.