Managing the financial implications of the termination of a contract

by Luc Marty, France

Albert the Furst of a longstanding commercial partnership (more than 60 years) the contract binding our client, an international oil company with an international oil corporation and its subcontractor had to be terminated in order to comply with European legislation affecting competition.

The abrupt termination of this contract resulted in a claim for compensation for breach of contract amounting to more than €1.5 billion.

The ad hoc arbitration proceedings initiated by the claimant required expert financial analysis of the opposing party’s demands with particular attention requiring to be paid to the diversity of the potentially overlapping issues of both immediate loss and loss of future revenues.

Above and beyond carrying out a financial and accounting review, Mazars also had to deliver an alternative assessment based on the economic reality, as of the termination date in contract with the claims which appeared to be based on inaccurate data and historical market information.

The reality of the situation was that the market had been experiencing continuous structural decline for many years.

Our challenge was, without placing any of the legal arguments in peril, to:

• Combine our financial arguments with those of the economic expert retained by our client to demonstrate the obligation of compliance with European competition law with which our client had been challenged;

• Respond to the technical issues posed by the necessity of achieving a valuation of the underlying business represented by the contract.

What form did Mazars’ contribution take?

Firstly, Mazars mobilised a team with the specialist skills required to perform a business valuation, an analysis of the contract’s economic model and an audit of the financial data provided by the claimant to support its claim.

Secondly, we were able to pinpoint the overlapping, or redundant, elements in both the claimant’s economic arguments and in its quantified demands. Our client’s legal team was able to use our conclusions to support and enrich its case.

Mazars had also to be able to demonstrate the implications of damages which were partly based on French accounting principles and methods to our English speaking client.

Finally, Mazars performed continuous assessments of the opposing party’s demands and also provided our client’s group management with regular appraisals of the probability of obtaining acceptance by the arbitration tribunal on particular financial issues (and then by the financial expert appointed by the arbitration Tribunal to report on certain specific points). Mazars provided the arguments by working alongside the client’s technical departments. By keeping the client’s management team informed at all times, they were able to judge whether to go ahead with legal proceedings or whether to search for a compromise. Because it could be demonstrated that the quantification and evidencing of the claimed loss was not robust, and because of confidentiality reasons, the solution of a compromise agreement was finally sought.

Please get in touch...
Introduction

These are challenging times for the world economy but, with some notable exceptions, the deluge of credit crunch or global downturn related investigations and disputes does not yet appear to have materialised. There are, however, signs that this may be about to change. With that backdrop, I hope this selection of articles will provide something for your thoughts.

Feedback and E.O. subscription requests can be sent to chris.drew@mazars.co.uk

Instructing the winning team

By Christopher Drew, UK

Experts are often seen as solitary individuals operating in their own specialist discipline. However, within Mazars we are seeing an increasing need for experts to interact and work together.

Mark Taylor, a Partner in London’s Forensic and Investigation Services team, is often appointed as a quantum expert alongside a liability expert, and asked him what he considered the consequences of a lack of dialogue between the experts could be.

“I was instructed several years ago on a case where a liability expert was also instructed. The instructing solicitor kept us apart - I never met the liability expert. I never corresponded with him, and I think if I had, I might have seen some of his initial work which I had relied in my report and considerable last minute searching was required.

The relationship between experts is often intensive - acting as a quantum expert I rely on assumptions provided by other experts. If I don’t have a thorough understanding of how those assumptions have been derived, or the liability expert doesn’t appreciate the use I intend to put them to, then there is a serious risk if the assumptions not being fit for purpose. I have recently acted as quantum expert on a series of shipping cases where I have liaised closely with the liability expert. By working together, often spending a lot of time together in the same room, we both fully appreciate each other’s roles and can take that into consideration when drafting our individual independent reports. In my opinion this worked particularly well as we were using evidence which was derived on a quantum level. I certainly believe that our understanding of what each other was doing made Counsel’s job a lot easier.”

Brian Dye of Excess Court Chambers was Counsel on that job and he agreed.

“In one of my recent cases where it went to arbitration, the experts gave concurrent evidence. The Tribunal was keen to obtain the input of the opposing experts together during expert testimony and, as a result, my industry expert and my quantum expert (Mark Taylor) were dealing with evidence and giving opinions in relation to the other side’s expert, actually during my cross examination of the expert. This enabled the Tribunal to deal with each issue in a logical way, looking at all expert evidence on it at the same time. This reflects a system embraced in Australia of ‘hot tubbing’ where all the experts testify together. In this scenario it is critical that the experts speak to each other and interact seamlessly, and they can only do this where each expert knows the other’s position intimately. Fortunately for my client, during this process which had been agreed both between the lawyers and the Tribunal, Mark and my industry expert acted symbiotically, gave robust and coherent evidence and were extremely impressive.”

Enquiries for expert witness assignments often come into the Forensic and Investigation Services team that require, for example, detailed GAAP knowledge or a practitioner’s opinion. Whilst the forensic accountants in our group have extensive experience of dispute resolution and have intimate knowledge of the proceedings and the systems, they readily acknowledge when there is a need to call on the expertise of partners from other groups in the firm.

Nigel Grummitt often works alongside other partners from Mazars who have been appointed as expert witnesses or expert adviser, and so I asked him about his experiences.

“I am instructed on many accounting or audit related topics, often in the context of professional negligence cases. However, I also acknowledge there are some real industry experts within Mazars who may have more expertise than myself in particular areas. In those situations we work together - we put forward the real technical expert as the expert, and we use the expertise of my forensic group to ensure that the expert performs to the client’s expectations, including a properly crafted expert report, and ensuring that the pitfalls of novice or inexperienced expert witnesses are avoided. At any one time we might be supporting a number of experts from Mazars - currently I am working with Paul Forrest from our Transaction and Consulting Services group, with Avril Whitfield from our Tax group and with Steven Brice from our Financial Reporting Advisory unit. Together we make a formidable team.”

Therefore, whilst choosing the right individual expert is clearly crucial to the chances of success, perhaps even more significant is how experts work together and communicate. Good communication and teamwork transforms individually accomplished experts into a winning team.

A needle in a haystack

By Christian Muehl, Germany

The collapse of the governance framework in India’s fourth-largest IT firm (Satyam) earlier this year shocked in India have reacted. Not only have they shown considered restraint, rather than a typical knee jerk reaction, they have also been highly engaged in a re-engineering and risk management role before an incident arises. In the current economic climate, these evidently will only increase.

IT forensic practitioners are routinely engaged proactively to advise on fraud prevention and mitigation procedures. Such work is almost always a damage limitation exercise with the principal aim of ensuring business continuity. On the other hand, in the case of investigations there is often an ultrasound effect of the business in that typically the problem and preserving fragile digital evidence. All too often companies handling fraud incidents internally do not carry out the appropriate processes, thereby destroying important evidence or even increasing the impact of the fraud on the business.

Information is the most valuable asset. IT forensic practitioners are often called to investigate business and fraud. IT forensic practitioners are not only valuable assets to investigate fraud but ideally placed to mitigate risks by performing a proactive role before an incident arises. In the current economic climate, these incidences will only increase.

Nigel Grummitt, Partner Forensic and Investigation Services
T: +44(0)20 7063 4101
E: nigel.grummitt@mazars.co.uk

Forensic and Investigation Services
Nigel Grummitt, Partner
Nigel Grummitt, Partner

By Christian Muehl, Germany

A needle in a haystack

In the Indian landscape

By Monish Chattrath, India

The collapse of the governance framework in India’s fourth-largest IT firm (Satyam) earlier this year shocked not only its clients (which included 180 of the Fortune 500 companies), but also sent the IT industry reeling as companies became wary of hidden skeletons emerging from the closets of other Indian IT firms.

It has been encouraging to see how the law authorities in India have reacted. Not only have they shown considered restraint, rather than a typical knee jerk reaction that one often sees when corporate scandals emanate from abroad like these megabanks, but they have acted swiftly to take the necessary corrective action to put Satyam back on track.

This began with the Indian Prime Minister deciding that Satyam was too important to India to fail and, therefore, its rescue should not be delayed by inquiries into India’s largest corporate fraud. This was followed by the appointment of a new board of directors. The Indian Company Law Board approved significant waivers that enabled the new directors to get to the bottom of the fraud by reconstructing deleted emails, which resulted in a confession by the fraudster, and resulted in him being convicted of a €5 million fraud.

Potentially more damaging to a company than deleting smoking gun emails in an attempt to conceal certain transactions is the deletion of valuable records and data. For example, an employee in his notice and leaves the building. It does not happen rarely that the individual not only takes his knowledge and expertise in his brain, but copies vital company data and deletes his emails and computer files to harm the former employer. Whilst the company’s IT department sometimes able to do a partial restore of the files, significant disruption is caused by the length of the time this takes.

IT forensic practitioners are routinely engaged proactively to advise on fraud prevention and mitigation procedures. Such work is almost always a damage limitation exercise with the principal aim of ensuring business continuity. On the other hand, in the case of investigations there is often an ultrasound effect of the business in that typically the problem and preserving fragile digital evidence. All too often companies handling fraud incidents internally do not carry out the appropriate processes, thereby destroying important evidence or even increasing the impact of the fraud on the business.

Information is the most valuable asset. IT forensic practitioners are often called to investigate business and fraud. IT forensic practitioners are not only valuable assets to investigate fraud but ideally placed to mitigate risks by performing a proactive role before an incident arises. In the current economic climate, these incidences will only increase.