The Continued Importance of Monitoring

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The Continued Importance of Monitoring

Due diligence inquiries provide investors or business partners with valuable information necessary to make informed decisions related to potential business transactions or relationships. After due diligence inquiries have been conducted, investors or business partners may wish to initiate monitoring to ensure no information has changed to negatively affect ongoing relationships. During the recent economic crisis, the financial stability of certain entities is constantly changing. In addition, regulatory actions and litigation filings can quickly change the reputation of a business entity. These types of changes highlight how continued monitoring is a useful tool to help protect investments and business relationships in a rapidly evolving business climate.

On April 16, 2009, Dow Jones Corporate Filings Alert published information regarding more than 60 public entities which have recently reported that circumstances have arisen, or could arise, raising doubt about their ability to continue as going concerns. One entity, American Axle & Manufacturing Holdings, Inc., disclosed that its auditors recently raised doubts about its viability because of the uncertainty surrounding its two largest customers, General Motors and Chrysler. In 2007, American Axle reported net earnings of US$37 million. However, for the first quarter of 2009, American Axle reported a net loss of US$32.7 million. American Axle's recent negative financial performance and exposure related to General Motors and Chrysler have been well documented in the media as well as U.S. Securities and Exchange Commission filings. Investors or business partners of American Axle would benefit from monitoring the media and regulatory filings to stay informed of the entity's current and future financial situation.

The monitoring of actions taken by regulatory agencies is also a valuable tool to investors or business partners. In early May 2009, New York Attorney General Andrew Cuomo announced a nationwide investigation into the debt settlement industry. On May 19, 2009, Cuomo's office filed a lawsuit against debt settlement entity Credit Solutions of America. Prior to this lawsuit, limited information was available regarding this entity in media and litigation databases. Thus, due diligence inquiries prior to May 2009 would likely have resulted in no overly adverse information regarding regulatory violations, investigations, or litigation. An investor or business partner of Credit Solutions of America may not learn of the recent litigation filed against the entity without actively monitoring the activities of the entity. Often, a lawsuit filed by an attorney general's office leads to various class-action lawsuits and/or additional regulatory scrutiny, which can negatively impact the entity's reputation and financial performance.

Monitoring is also a useful way for investors or business partners to stay informed of the current status of litigation or negative regulatory events found during the course of initial due diligence inquiries. If an entity was found to be involved in numerous litigation matters, investors or business partners should consider monitoring these litigation matters until any pertinent matters are resolved. This monitoring can be useful in determining any monetary responsibility ordered to be paid by the entity in question. In addition, an entity found to be the subject of past regulatory infractions should be monitored for ongoing compliance with the appropriate regulatory agencies. Minor regulatory violations may often lead to controversial issues that become highly publicized, which can impact an entity's reputation.

Monitoring is also a method of determining if the decision-makers of an entity remain the same as when initial due diligence inquiries were conducted. If investors or business partners enter into a business transaction with an entity consisting of a certain management team, the same investors or business partners should be interested in learning if these decision-makers leave the entity. While many executives retire or move on to other opportunities, the resignation of CEOs or CFOs is often a warning sign of possible problems within an entity. In August 2006, Willbros Group announced the resignation of its CFO on the same day the entity announced the settlement of a class-action lawsuit accusing the company and three present and former officers and directors of making a series of false and misleading statements and of a scheme to defraud investors.

In the midst of the current economic crisis and during a time when regulatory and media scrutiny is increasing, post-due diligence monitoring remains a valuable tool to ensure that business transactions, relationships, or investments are not jeopardized. Monitoring provides powerful insight and indicators of the current standing of a potential business partner. This up-to-date insight acquired through monitoring provides investors and business partners with the knowledge they need to make informed, real-time decisions to grow their businesses and minimize their risks.

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