



# The impact of Covid-19

The economic downturn and the vulnerability of SMEs from Serious Organised Crime

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# What's the Background?

Latest forecasts from the Organisation for Economic Co-Operation and Development (OECD) show an increasingly negative impact of the pandemic on global GDP growth. Surveys since February 2020, show that Small Medium Enterprises (SMEs) and entrepreneurs (less than 250 employees) are extremely worried about the impact of COVID-19 on their financial reserves and business survival. This is no different in Scotland.

Recent surveys show that there are approximately 344,000 SME's operating in Scotland, accounting for 99.3% of all private sector firms. Together they employ around 60% of the Scottish workforce. In other words, SME's dominate the Scottish business population, so how these firms survive, adjust and adapt to the Covid-19 crisis will have an enormous bearing on future economic and society's welfare in Scotland for years to come. UK SME figures suggest that there are potentially 120,000 UK small businesses (known as micro firms with less than 10 employees) at immediate risk of a 'financial crisis' if they cannot generate a revenue stream for a few months.

## WHY ARE SMES MORE VULNERABLE?

The Pandemic has affected both larger and smaller firms, though the impact on SMEs is especially severe, particularly because of higher levels of vulnerability and lower resilience related to their size. Comprehensive evidence suggests the firms likely to experience the greatest impact from shock events are SMEs.

The dramatic and sudden loss of demand and revenue for SMEs severely affects their ability to function, and/or causes severe financial shortages. Furthermore, consumers experience loss of income, fear of Covid-19 and heightened

uncertainty, which in turn reduces confidence, spending and consumption. These effects are compounded because workers are laid off and firms are not able to pay salaries, therefore adding to the issue.

Over the longer term, it may be difficult for many SMEs to re-build connections with former networks, once supply chains are disrupted and former partners have set up new alliances and business contracts. As a result, many Scottish SMEs may become vulnerable.

## EXAMPLES OF SME VULNERABILITIES

- SMEs may have less resilience and flexibility in dealing with the costs these shocks entail (Low cash reserves)
- Costs for prevention as well as requested changes in work processes, such as the shift to teleworking, may be relatively higher for SMEs given their smaller size
- In many instances, the low level of digitalisation and difficulties in accessing and adopting technologies are problematic for SMEs
- If production is reduced due to lower demand, the costs of underutilised labour and capital weigh greater on SMEs than larger firms
- SMEs may find it harder to obtain information and implement measures to halt the spread of the virus
- A struggling business with a good local standing is a prime target for SOC investment

## THE SERIOUS ORGANISED CRIME MODEL AND WHAT THIS MEANS TO VULNERABLE SMES

Serious Organised Crime Groups (SOCG's) in Scotland are involved in a diverse and wide range of known and emerging criminality that includes drugs, violence and fraud. They also engage in money laundering, the importation, storage and supply of firearms, human trafficking, immigration crime, counterfeiting, acquisitive crime (including fraud), environmental crime, sexual offences, Child Sexual Exploitation, and extortion.

Many Serious Organised Crime enterprises result in illicit gains including vast amount of cash, which they have to launder to avoid Proceeds of Crime Act recoveries. They do this by disguising and mixing criminal cash behind the front of an apparently legitimate company. The company can become a vehicle for money laundering.

## THE RESPONSE TO COVID – 19 BY SMES

As many businesses struggle due to financial hardship, they will seek out possible business strategies to lighten the shock, and look to government initiatives, deferred tax payments, business rate relief and bounce back loans to provide support. When these legitimate options have been exhausted, SMEs may become desperate and look for quick and risky solutions they would not have previously considered. Beware of the ever present threat from SOC as they move in to fill that funding gap and offer very attractive investment deals or loans. SMEs should be aware of the old adage:

**‘If it appears too good to be true – it probably is.’**

This is particularly relevant to cases where the company that is struggling has a good trading record, is well known locally and in particular, has ongoing public sector/local government contracts. Some of these businesses will be vulnerable with their cash flow hit and balance sheets under pressure. The temptation to sell out to apparently cash rich buyers - or to take on an investment or ‘Business loans’ from them - is likely to be irresistible to some.

## THE RISK OF ENGAGING WITH SOC LINKED BUSINESSES

- SOC linked businesses have funding models that have the advantage of criminal cash behind them. This enables them to facilitate unfair attractive bids when applying for contracts.
- The presence of a SOC linked company will squeeze out legitimate local competition
- While the new business runs in the foreground, Serious Organised Crime runs in the background. The new business is linked to this and therefore supports the SOC business model

- The new SOC linked business will be used as a front to conduct criminal activities behind the guise of a legitimate business. Cash, drugs, weapons, stolen goods and victims of human trafficking all need moved around. Will your business be used to do this?
- The new SOC linked business may be used to launder criminal proceeds through clever accounting
- As well as money laundering, your business may be used to indulge in shortcuts, unscrupulous or fraudulent activity all designed to maximise profit margins at the expense of hard earned business ethics and integrity
- Maximising profit margins is often at the expense of others, including the exploitation of human beings through human trafficking or modern slavery.
- As owner, Director or shareholder – There is a fairly good chance that you may lose control of your business
- The profits from the new business may be used to fund further other serious criminality – thus completing a ‘vicious circle’ and adding to the misery that SOC brings to local communities
- Much of the above activity will gain the attention of law enforcement agencies and you may become involved in criminal investigations

## SUPPORT FOR SMES

Careful consideration should be given to seemingly lucrative opportunities. Support is available from a number of sources (not exhaustive);

### Scottish Business Resilience Centre

<https://www.sbrcentre.co.uk/>

### Scottish Government support

<https://www.gov.scot/publications/coronavirus-covid-19-support-for-businesses/pages/business-support-fund/>  
<https://findbusinesssupport.gov.scot/>

### Scottish Enterprise

<https://www.scottish-enterprise.com/support-for-businesses/coronavirus-covid-19-advice>

### UK Government

<https://www.gov.uk/guidance/coronavirus-covid-19-information-for-individuals-and-businesses-in-scotland>

### Citizens Advice Scotland

<https://www.cas.org.uk/>

## OTHER USEFUL LINKS

### Find your local council

<https://www.mygov.scot/find-your-local-council/>

### Police Scotland

<https://www.scotland.police.uk/>

### Crimestoppers

<https://crimestoppers-uk.org/>

### Scotland's Serious Organised Crime Strategy

<https://www.gov.scot/publications/scotlands-serious-organised-crime-strategy/>

Given the rapid pace of developments, the overview of the impact of Covid upon SOC is not a comprehensive position and as such responses to this and what this means for SMEs are still very much a work in progress. This alert is the 1st response to this issue and will be updated accordingly.

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