

A background image showing two men in business suits and ties, looking towards the left. The man in the foreground is wearing glasses and has a serious expression. The man behind him is also looking in the same direction.

## Contract Compliance reviews: Enhancing the bottom line with more efficient management

ADVISORY

Companies are under increasing pressure to improve their bottom lines. Yet despite this, part of their income constitutes a risk since sometimes vendors, distributors and licensees fail to meet their contractual obligations in full. Most business partners do not do this deliberately. Mistakes can be attributed to the complex nature of a contract, a lack of resources, or quite simply a lack of clarity surrounding the roles and responsibilities set out in the contract. Based on the experience of reviews conducted by KPMG, payments of license fees or royalties can fall up to 10 percent short of the values stipulated in their corresponding contracts, while 90 percent of self reporting can also be incorrect if it is not properly managed.

### How can I help?

KPMG's Internal Audit services not only comprise a review of license contracts and those managed by third parties, but also protect intellectual property. Part of our service involves providing advice with a view to developing and maintaining a more transparent and more efficient system of controls. Operating a control system after the review has been conducted reduces the level of risk and helps facilitate the collection of revenue that was previously unaccounted for.

### Contact compliance reviews

#### **Review of license and royalty contracts**

Companies generally do not manage the income derived from royalty and license contracts as actively as they do in respect to other sources of income, while responsibility within the company is divided between the finance, sales and legal departments. There is one further obstacle to efficient management. Companies tend to manage royalty and license contracts by means of self reporting. Unless the company instructs its contractual partners at an appropriate level of detail, self reporting can be a source of error. Inaccurate self reporting is generally not intentional and can be caused by complex contractual conditions, incorrect completion or by a lack of clarity surrounding the responsibilities of the person entrusted with the self reporting process. The company can also benefit from:

- the systematic management of license and royalty income
- individuals independent of the company conducting the review, which preserves business relations and helps to avoid any differences of opinion
- contractual partners becoming used to the practice of regular and systematic self reporting.

### Review of distributor and other vendor contracts

Companies often conclude complex agreements with their distributors and other contractual partners. Agreements governing the division of profits are commonplace in joint ventures, while in respect to distributors one often sees incentives built around bonuses and rebates. When outsourcing production, contracts can include cost transfer options or clauses relating to other profits and which depend on the size of production. Reviewing contracts also helps to prevent the company from relying solely on the financial system of its business partners and enhances the importance of self reporting.

### Review of business partners

Contractual relations between companies and their business partners can deteriorate or undergo change when a company is bought up or a holding is sold. Part of our review involves analyzing these business relations and reviewing the details. Subsequently we recommend the steps which could be taken to rebuild the previous relationship and restore the communication and trust which prevailed before the dispute.

### Protection of intellectual property

#### Management of intellectual property

Since the introduction of the Sarbanes Oxley (SoX) Act, responsible corporate management in the broader sense has been expanded to incorporate aspects which traditionally played no part here. An increasing number of companies have recognized the importance of actively managing intellectual property (IP) and raising its value. Poor management of intellectual property can

cause legal problems, squandered research and development expense, lost competitive advantages or even financial underperformance. KPMG's Intellectual Property services help in devising an appropriate strategy, managing costs and protecting intellectual property from competitors. Our IP service team works together with financial, taxation, legal and other experts. The company can also benefit from the following:

- The efficient management of IP enhances its value and provides a competitive advantage for the business
- Tax efficiency related to IP increases while tax payment liabilities fall
- Communication improves with shareholders and other business players after the implemented changes are communicated to them
- Greater liquidity and easier access to the capital markets
- Proactive management (sale, purchase) of IP assets required for future growth.

### KPMG methodology

Our Internal Audit services are continuously adapted to client demands and focus on the following:

- Extensive professional experience in the traditional and ground-breaking fields of internal audit services
- Ongoing co-operation with the company management and departments of KPMG furnishing other services
- Use of automated internal auditing tools right from the start
- The global professional background to KPMG's internal auditing methods means that rapid responses can be given to any questions that arise.

Our service is built around continuous and personal contact with the client and seeks not to disturb the day-to-day business processes of the company.

### The next step

KPMG in Hungary draws on its global background as part of a network of professional services firms in providing internal auditing services that are extremely diverse. More information is available on the outsourcing or co-sourcing of internal auditing as well as on the details of the K'Sprint service enhancing the value of internal auditing and the Enterprise Risk Management (ERM) service.

We would also be pleased to meet you in person, to tell you more about what we do.

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