KPMG

KPMG International Annual Review 2006

Client focus

KPMG INTERNATIONAL

AUDIT ▪ TAX ▪ ADVISORY

Client focus

Understanding the issues clients face is critical to being able to deliver any of our Audit, Tax or Advisory services. As a multidisciplinary business, we look to have deep industry knowledge embedded in all parts of our member firms but equally recognize there is often value to be gained by sharing ideas and experiences across industry sectors. Clients can learn a lot from how companies in other sectors deal with particular issues. One of our roles is to make sure we bring this knowledge to both large and mid-sized companies to help them develop and expand their businesses.

USD8.3billion

Combined revenue of Audit Services in KPMG member firms in 2006

BASF

BASF is one of the world's leading chemical companies. Its portfolio ranges from chemicals, plastics, performance products, agricultural products and fine chemicals to crude oil and natural gas. As a reliable partner to virtually all industries, BASF's intelligent system solutions and high-value products help its customers to be more successful. BASF develops new technologies and uses them to open up additional market opportunities. Its economic success is founded on a strong commitment to environmental protection and social responsibility. BASF has over 95,000 employees and posted sales of more than 42.7 billion euros in 2005.

At the BASF Annual General Meeting in May, KPMG in Germany was appointed as the sole external auditor to the group in what was one of the most significant wins for our German member firm in recent years. Our teams are providing a full integrated audit for BASF and KPMG firms are now serving the client in 90 countries with Germany, the U.S. and China being the main areas of activity.

This important win reflects the fact that we listened carefully to the client's requirements and came up with a proposal that included tailored strategies to meet its needs. To help us we are using a newly developed customer relationship management system.

PETROBRAS

Petrobras, the Brazilian energy group, has grown since its creation just 53 years ago to become Latin America's largest corporation by market capitalization. We were keen to work closely with this South American giant in the international oil and gas sector as it matched both the growing international presence of our Energy and Natural Resources network and our decision as a network to focus on the region as a prime target for growth.

When Petrobras began the search for a new external auditor, we faced tough competition. But we were able to build on a relationship with the company and drew on the experience and knowledge of 20 KPMG member firm offices in the region and in Europe and Africa, where Petrobras has a presence. We were also able to use our Oil and Gas Center of Excellence in Rio de Janeiro to demonstrate our leadership in the energy sector.

In 2006 KPMG in Brazil won a gruelling contest to become the external auditor. Revised fees, negotiated in accordance with Brazilian tender law, were agreed and in April the Petrobras board gave the green light for our appointment. Subsequently we have been asked to submit proposals to work with Petrobras in 10 other countries.

HUAWEI

Founded in 1987 in the southern boom-town of Shenzhen, Huawei is one of China's most prominent success stories.

Privately owned, the company is the largest domestic telecommunications equipment manufacturer in China, and, unlike many other large Chinese enterprises, is at the front of the new wave of "outbound investment"—wealthy Chinese firms that are investing in markets overseas.

For Huawei, this strategy is paying off. More than half its revenue now originates outside of mainland China, from relatively mature markets such as Western Europe, Australia and Hong Kong SAR. Huawei serves 28 of the world's top 50 telecommunications network operators, and has successfully installed 3G networks in Hong Kong and the UAE—popular networks that see heavy use.

KPMG member firms began working with Huawei in 2000, when the company recognized the need for a high-quality audit. We currently provide audit services for the company across China and the rest of the world and regularly carry out transaction services work for key acquisitions or divestments.

The key to KPMG's enduring relationship with Huawei has been our active, year-round communication with the group and the continuity and coordination of our global team—particularly important as Huawei executives head overseas to manage new operations. We also provide accounting seminars and updates to help the company improve its internal controls and continue to look for new ways to support the client internationally.

USD**3.3**billion

Combined revenue of Tax Services in KPMG member firms in 2006

HM REVENUE & CUSTOMS

There is a clear value in the private sector and government working together to help businesses generate even greater economic growth for a country. For example, the U.K. government is searching for ways to cut the cost of regulation for U.K. businesses. Against very strong competition, KPMG in the U.K. was appointed by Her Majesty's Revenue & Customs (HMRC) to support this initiative by measuring the current administrative burdens created by the tax and duty system.

The project, which concluded in March 2006, involved the most complex application of the standard cost model—an activity-based costing methodology—undertaken anywhere in the world. The work involved a team of more than 100 KPMG professionals and a 200-person call center.

Having identified all of the obligations imposed by the tax and duty system, KPMG teams interviewed 1,000 businesses of all sizes to define the time spent and costs incurred in meeting obligations. An advisory board was appointed to ensure that business representatives were involved in both the process and the work products.

Against a very tight deadline, KPMG professionals delivered a large report and a huge data framework of more than 2.5 million data points, with targets for administrative burden reductions that were set in the government's 2006 Budget.

GROSVENOR

Grosvenor, the privately owned international property development, investment and fund management group, is best known for its substantial real estate interests in central London. However, it has regional operating companies in Australia, Asia Pacific, the Americas, Britain and Ireland and Continental Europe with an international property fund management business across these regions. With 12 offices around the world managing interests in 17 countries either on its own account or held through joint ventures and funds, the group has become an important global client for KPMG firms.

KPMG has acted as the group's tax advisers since the mid-90s, and we were reappointed to this role at the beginning of 2005. We have worked with Grosvenor to develop their group tax policy and helped them roll it out around the world.

Grosvenor's tax policy is to pay its fair share of taxes wherever it operates, backed by excellent compliance processes. Recently we mapped these processes with Grosvenor and helped identify areas for improvement.

KPMG firms have has built strong working relationships with Grosvenor globally and this has extended to other Advisory work with the client. Recently we carried out financial and tax due diligence for the group when it increased its stake in the Spanish retail development group, Sonae Sierra. We provided similar advice with respect to Grosvenor Fund Management's acquisition of Legg Mason's U.S. real estate fund management operations. We advised on the investment structure behind Liverpool One—one of the largest urban regeneration projects in Europe—and have supported the group with advice on structuring new investment funds and property acquisitions in Australia, the U.S., Spain and the U.K.

TELEFÓNICA

Telefónica is one of the world's top five telecommunications companies offering a complete range of fixed, mobile and Internet services to some 192 million domestic and business customers in Europe, Latin America and Africa.

Rooted in Spain, it now has a larger proportion of its business outside its home market. Determined expansion in the last 15 years has seen it become the leading player on the increasingly vibrant business axis between Iberia and Latin America. It is the leading operator in Brazil, Argentina, Chile and Peru and a substantial presence in most other countries in the region including Colombia, Mexico, Uruguay, Panama and Venezuela. Its European operations now also incorporate the O_2 mobile phone business in the U.K., Ireland, Germany and the Czech Republic and it has won a license to operate in Slovakia. The company employs nearly 150,000 people.

We have worked closely with Telefónica on a number of big projects in the last three years bringing together an international team to match its growing footprint in key markets. Tax and Advisory partners from KPMG member firms in Spain, the U.K., Germany, Brazil and the U.S. have carried out due diligence on the acquisition of BellSouth in Latin America, advice on the merger with Terra Networks in Spain and the integration of Telefónica Móviles. The team has also provided Sarbanes-Oxley advice for O_2 in the U.K. and Germany and due diligence services in the U.K., Brazil and Argentina.

USD**5.3**billion

Combined revenue of Advisory Services in KPMG member firms in 2006

ADVENT INTERNATIONAL

Advent International, the global private equity (PE) house set up in 1984 to invest internationally, set up the world's first global fund in 1987 and has grown to be one of the biggest players in PE with operations in 24 countries. It now has more than USD10 billion of committed capital from more than 200 institutional and corporate investors in some 500 companies.

Advent specializes in buyouts, recapitalizations and equity investments in both developing and emerging markets. Its GPE IV fund, set up in 2001, raised 2.1 billion euros. GPE V, which closed in 2005, raised 3.3 billion euros.

Advent International won a record-breaking four industry awards at the fourth annual European Private Equity awards, organized by the EVCA, *Real Deals* magazine and INSEAD in 2006.

KPMG firms had worked intermittently with Advent in the past, but in 2002 decided they wanted a deeper and more lasting relationship. Our ability to offer a seamless global service—across Audit, Tax and Advisory work—formed an important part of our pitch, as did our promise to put our strongest partners and their teams at Advent's disposal.

The 2002 acquisition of MACH SA, a Luxembourg billing services group, was the first deal on which we worked, with a team involving people from our U.K., Luxembourg and U.S. member firms. A string of other deals followed including the management buyout of FD-International, a communications group; the Dutch Radio station, RD 538; and Parques Reunidos, a leading European amusement park, the first public-to-private PE deal ever done in Spain. Each time, we drew together teams with global and local knowledge.

On the strength of the work, we were invited to tender for Audit and Tax compliance work on all 80 of Advent's funds. A team drawn from the U.K. and U.S. won the bid and since then the relationship has grown stronger still. Today we are serving Advent in 21 countries. In the last two years we have advised on a range of Advent initiatives including the formation of several new funds; acquisitions in Mexico, Brazil and Uruguay including the Nuevo Banco Commercial; and acquisitions across Central, Eastern and Western Europe.

DEPARTMENT OF ENERGY, GOVERNMENT OF MADHYA PRADESH AND STATE DISTRIBUTION UTILITIES

India's Electricity Reform Act has prepared the way for a fundamental restructuring of the country's power industry.

In the state of Madhya Pradesh the previously vertically integrated electricity board has been broken into a power generation business, a company running the transmission grid and three licensed distribution companies that have a direct interface with customers. These companies are now readying themselves for further deregulation in the market.

A team of 20 KPMG professionals, drawn from all functions within our Advisory services team, is now working with the three distribution licensees to make sure they are properly supported in building capacity and in commercializing their operations. Our firms are helping them complete industrial and financial restructuring, supporting the introduction of new technology and preparing their people for the challenges of deregulation with a particular emphasis on greater customer focus.

The team, part of a consortium, is operating out of the head offices of the three companies in Bhopal, Jabalpur and Indore. The assignment is expected to last three years.

TAKEDA PHARMACEUTICAL

Takeda is Japan's largest pharmaceutical company and a leading player in the international industry, developing a wide range of products for such conditions as prostate cancer, peptic ulcers, hypertension and diabetes. The company's aim is to strive for improvements in individual health and progress in medicine. Based in Japan, Takeda has marketing and research operations across the world and a strong emphasis on producing ethical drugs.

Over 40 years, from the days of Peat Marwick, KPMG firms have built a strong and trusted relationship with Takeda, bringing together the skills and knowledge of professionals not just in Japan but in the U.S. and Europe to support the company. Strongly led from Japan, the KPMG team is a close-knit group drawn from across the KPMG global network.

Our member firms have provided a range of services including internal audit advice for key overseas subsidiaries in the U.S., Ireland, the U.K., Germany, France, Taiwan, the Philippines and Indonesia. Our member firms have also provided Tax advice and Advisory services for the introduction and operation of new internal control disclosure requirements in Japan. This work has now been expanded.

IBM

For almost 100 years, IBM's products and services have been revolutionizing global businesses.

IBM is the world's largest information technology company, recording global revenue in 2005 of USD91.1 billion. In revenue terms, it is the world's biggest provider of IT services, hardware and financing, and second in software. IBM has approximately 329,000 employees serving clients in 174 countries. With approximately 190,000 professionals, IBM's Global Services is one of the world's largest providers of IT services and consulting.

IBM's business model hinges on one word: innovation. It brings deep insight to bear on issues, processes and operations across industries and invents technology to help clients meet challenges and solve business issues.

IBM is an important KPMG Advisory and Tax client with an international team of more than 200 active professionals with lead partners in Asia Pacific, Europe and the Americas. KPMG has established strong relationships with IBM professionals around the world and continues to build and enhance relationships in key service areas in 35 countries and in multiple businesses and functions.

KPMG's member firms provide a range of services in the following areas: Tax, Transaction Services, Forensics, Contract Compliance, Operational Risk Management and Information Risk Management. KPMG's member firms also work with IBM's Global Business Services to provide joint services to clients across multiple industries.

Consistency of work product, well-established and experienced teams with global delivery capability and a single point of contact have all contributed to the KPMG network's success with this important global client.

Photograph: Guy Nicolas

SOCIÉTÉ GÉNÉRALE

Société Générale, one of France's largest banks, has in the last 10 years become a key player in the international financial services industry with a presence in more than 75 countries and a market capitalization of some 60 billion euros.

KPMG has worked closely with Société Générale in many countries and across its different businesses. We have helped the bank grow in new banking markets such as Russia, China and India, and have provided advice on tax and employee services as well as risk management advice for both its investment and corporate banking businesses. In France and abroad, we have also assisted the bank in implementing IFRS and introducing Basel II reforms.

But the relationship grew deeper in 2006 when the bank asked us to sign a global service agreement which would match its increasingly global footprint. This has allowed us to rethink how we serve this client around the world and to map the strategies we provide the bank much more closely against its challenges and needs.

Société Générale and KPMG share a common view of how our relationship should develop. We are both key players in our respective markets and we want to benefit from each other's knowledge and experience. Our strong market position and deep understanding of the financial services sector underpins our commitment to provide consistent high-quality service to Société Générale. We have been amazed at the increased value we can bring to the bank when we properly understand the issues it faces, not least by selecting a strong and talented Advisory team to meet its needs.

ABSA

ABSA is one of South Africa's most powerful financial services companies, offering a full range of retail, commercial and corporate banking, insurance and other financial products. It has assets of approximately 470 billion Rand and serves 8.1 million customers through 727 branches, employing just under 35,000 people.

ABSA also serves other selected markets including the U.K., Angola, Mozambique, Tanzania and Zimbabwe. Since July 2005, ABSA has been a subsidiary of Barclays.

Following the Barclays acquisition, KPMG resigned as one of ABSA's joint statutory auditors with the agreement of the bank's senior management. Instead we were officially appointed as the preferred provider of a wide range of non-audit services at the group's Annual General Meeting.

Services offered since then include implementation of a Sarbanes-Oxley controls framework, external financial reporting, financial risk management, transactions advice, corporate finance, internal audit, forensic services and technology advice.

TOSHIBA

During the year we assembled an international multidisciplinary team to act as sole financial adviser to Toshiba in its USD5.4 billion acquisition of nuclear engineering company Westinghouse from British Nuclear Fuels (BNFL).

The KPMG team was mostly drawn from the U.K., Japan and the U.S. firms but colleagues in Belgium, the Czech Republic, China, France, Germany, Slovenia, Sweden, Switzerland and the Ukraine also lent their support. The team involved professionals offering skills across a wide range of disciplines including corporate finance, valuations, transaction services, human resources and tax.

The deal—which helped Toshiba become a major global player in the nuclear industry—was the biggest ever advised on by the corporate finance practice of an accounting organization. It was also one of the most significant overseas transactions by a Japanese corporate in more than six years.

KPMG became aware of BNFL's intention to sell Westinghouse in 2004 and started researching potential buyers. Following discussions with the KPMG team in Japan, Toshiba Corporation was identified as a good fit because of its ambitious plans to expand its locally strong nuclear systems business internationally. We approached the company and went on to become sole financial advisers in the acquisition of Westinghouse.

This was a complex deal that saw a Japanese company take control of the U.S. subsidiary of a U.K., state-owned company. Our deep industry knowledge and ability to provide an integrated global service added value for the client in this important transaction.

QZINA

One of the most difficult hurdles for any growth company to overcome is deciding when best to invite outside investors in and give up outright family or founder ownership.

KPMG in Canada had been closely involved with Qzina, a family run importer and distributor of fine food products, including gourmet chocolate and specialty dessert ingredients, from its inception in 1996. After nine years the company had grown significantly, was generating positive earnings and needed new investment to expand. But only one of the three founding brothers wanted to continue leading the business; the other two were looking for an exit.

KPMG was called in to find suitable investors and guide the company through the sale process, including negotiating share purchase, shareholder and employee agreements.

The business was acquired by HSBC Capital (Canada) with the active brother retaining a 25 percent stake in the business. Supported by HSBC's financial expertise and resources, he is now able to steer the company through to its next phase of development. This includes working with KPMG Transaction Services teams to take on a significant U.S. acquisition, which could increase revenue and earnings by 30 percent. The two other brothers were able to realize their investment.

R. GRIGGS GROUP

Failure to respond to changing fashion and manufacturing trends had put the makers of the iconic Dr Martens shoes and boots brand—R. Griggs Group—on a perilous course of declining sales and mounting losses.

Sales fell by GBP100 million to GBP130 million in just four years while the business racked up losses of GBP103 million. By mid-2002, the group was six months away from running out of cash.

KPMG in the U.K. was brought in to devise a radical recovery plan for the business in just 12 weeks. Working alongside a new chief executive, we aligned management and helped convince the bank to support the plan. The shareholders were also supportive with a GBP10 million equity injection to fund the restructuring.

All five U.K. manufacturing sites were closed and production was switched to Asia within five months, reducing headcount from 1,600 to 257. The range was refocused, design spend was increased and money was made available to rebuild the brand.

The result is that a world-class branded business has been saved and is now prospering under new leadership, with pre-tax earnings up to GBP5.4 million in March 2006 and gross margins up 16 points to 39 percent. New jobs are now being created and the business has been successfully relaunched in the U.S., previously its most successful market.

This impressive turnaround was recognized as the Private Company Turnaround of the Year for 2005 by the Society of Turnaround Professionals in the U.K..

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