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IN THIS ISSUE

EXPERTS FEATURED IN THIS ISSUE

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START-UP: A BUMPY ROAD TO SUCCESS?

Jerzy Kalinowski explains to "Turning Point" why innovations need start-ups.

TURNING POINT (TP) HOW WOULD YOU SUMMARIZE THE MAIN TRENDS IN ENTREPRENEURSHIP IN THE LAST YEAR?

JERZY KALINOWSKI (JK) » Innovations and start-ups: these two words dominated the world in 2016. In Poland the word "start-up" is now very "sexy" and it is often used in the context of a declaration "I have a business idea" or "I'm starting my own company". However, the term start-up that appeared with the first wave of the internet revolution in the first half of the 90's has a slightly different meaning.

TP: » THEN WHAT IS THE DEFINITION OF A START-UP?

JK: » A start-up is a company in its early phase of business development, that possesses (or creates) an innovative product or service or an innovative business or an operational model which give the company a potential for dynamic growth.

TP: » WHAT DOES A "DYNAMIC GROWTH" MEAN IN BUSINESS TERMS?

JK: » A company referred to as a start-up should have a very **dynamic growth** potential which is possible due to **business scalability** (income can grow much faster than costs) connected with an easy geographical expansion. An important feature of start-ups is the fact that these companies are still in the phase of development, in which they need external financing to reach their development goals. Gathering funds for development is a critical step for every start-up.

TP: » HOW DO YOUNG ENTREPRENEURS OBTAIN SUCH FINANCING? IT SEEMS TO BE A RATHER DIFFICULT TASK ON THE HIGHLY COMPETITIVE MARKET OF GOODS AND SERVICES.

JK: » The early stage of a new company is usually financed from the funds of its founders, their friends and families (*Founders, Family, Friends & Fools*). If the company develops dynamically, it soon faces the need of obtaining bigger financial performance. In that early phase it is almost impossible to receive a loan, so the options of financing are limited to the so-called business angels, venture capital or crowdfunding (Picture No 1, p. 8).

TP: » WHO ARE THE BUSINESS ANGELS AND WHAT EXPERIENCE DO THEY TAP INTO?

JK: » "Angels" are usually people between 35 and 60 years old who have available financial, entrepreneurial and multidisciplinary resources, as well as vast experience in management and a lot of business contacts. Such people are particularly eager to invest in projects in their neighbourhoods, in industries they know, often as a part of the so-called investment clubs in which a few people invest together and at least one of them is

A start-up is a company in its early phase of business development that possesses (or creates) an innovative product or service or an innovative business or an operational model which give the company a potential of dynamic growth.

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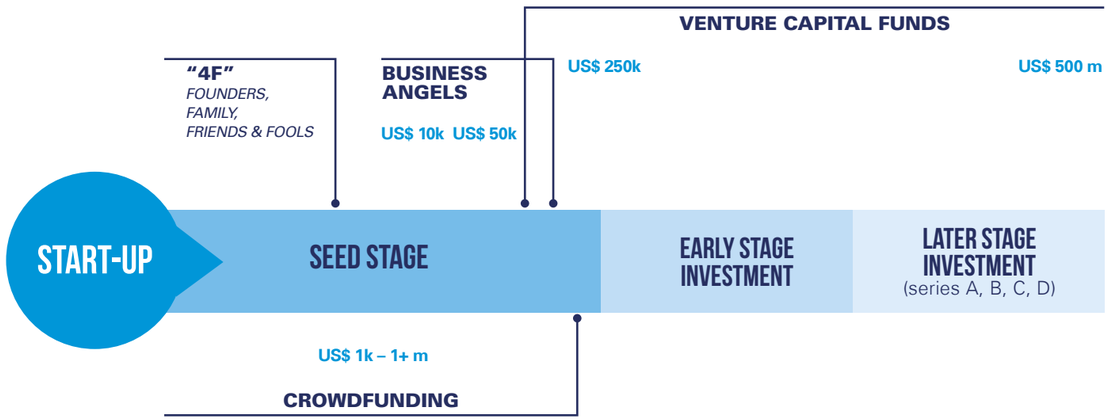
Jerzy has over 30 years of professional experience. He has worked at KPMG since 2004. During that time, has worked projects in the scope of strategic-operational consulting in almost 20 countries all over the world. Prior to joining KPMG, Jerzy was the member of management and supervisory boards of companies from the sector of new technologies, media and telecommunications (he was, among others, the founder and the chairman of VC focused on digital start-ups). His experience includes participation in research and development projects in the United States and Poland. He is a graduate of the Warsaw University of Technology and the University of Rochester in the USA.

Figure No 1

START-UP FINANCING SOURCES



TP: » WHAT DO THE INVESTORS GET IN EXCHANGE FOR THEIR FINANCIAL SUPPORT?

JK: » "Business angels" invest their money in start-ups. Their business goal is not only multiplication of the invested capital (a minimal expected return is the doubling of capital in 6 years) but also the commitment to support the companies they invest in. Entrepreneurs who created their own start-up are often reluctant to receive any external "intervention" for their business. But it's in their best interest to find a "business angel" who will not only make an investment but will also actively help in the development of products or services, in business scalability, in building the company itself or in finding new customers and business partners.

TP: » INVESTING IN A START-UP IS A MAJOR RISK. CAN POTENTIAL INVESTORS PROTECT THEMSELVES FROM LOSSES?

JK: » Upon making an investment "business angels" accept the high risk of the early stages of a start-up's development, and that's why before making the decision to invest they focus on risk analysis and possible means of risk mitigation. That's why entrepreneurs who seek the help of such an investor, should openly discuss even the most difficult aspects, bearing in mind that this kind of dialogue is the only way to get real support from their "angel". When acquiring a "business angel", entrepreneurs should also remember that the people who can facilitate funding in the future are particularly valuable.

TP: » APART FROM THE "BUSINESS ANGELS", IS THERE ANY ALTERNATIVE SOURCE OF FINANCING?

JK: » Investment funds are the alternative. "Business angels", however, are the most common form of *seed financing*. On the most developed markets, e.g. in the US, "business angels" every year fund 40 to 50 times more start-ups than venture capital funds do. Poland, however, is still in a rather early stage of start-up market development and the number of active "business angels" is fairly small, thus obtaining financing from them is a huge challenge for Polish start-up creators.

TP: » WHAT IS THE NATURE OF VENTURE CAPITAL FUNDS?

JK: » *Venture capital* funds are dedicated to financing investments projects with a huge growth potential, whose development is however fraught with high risk. Start-up owners who are trying to obtain financing should understand the investment strategy of the venture capital fund they want to "speak with". First of all, it should be the methods of the fund and the industry they invest in. It's worth to check in advance which phases of start-up development are "accepted" by the particular fund. Also a piece of information important from the investor's point of view is the minimal and maximal capital invested in a single company and the geographic area of investment.

IMPORTANT ASPECTS OF THE FUND'S "CONTRIBUTION" TO THE DEVELOPMENT OF A START-UP:

- **connections of the fund, which allow to reach customers and business partners,**
- **support in marketing and sales, that are crucially important to achieving the planned dynamic growth,**
- **an active support in business problem solving,**
- **aid in structural "organizing" of the company and its management system,**
- **access (through the fund) to supplementary external knowledge and new solutions,**
- **the fund's experience in "leaving" the investment or a successful gaining the next round of financing,**
- **potential mentoring and support in recruitment, team building and talent management.**

TP: » WHAT INTERESTING TRENDS AND CHANGES CAN BE OBSERVED ON INVESTMENT FUNDS MARKET?

JK: » From the perspective of start-uppers that develop products and B2B services, Corporate Venture Capital funds (*CVC*) is increasingly important. KPMG global analyses indicate (*KPMG Venture Pulse: Q3'16 Global analysis of venture funding*) that in the 3rd quarter of 2016 nearly 28% of start-up investments were carried out by those funds.

TP: » WHAT BENEFITS DO CORPORATIONS OBTAIN FROM THIS TYPE OF FUNDING?

JK: » Corporations use the "vehicle" of the CVC fund to obtain external innovative solutions. An investor in the form of a corporate investment fund is particularly interesting for start-ups that possess innovative products or B2B services. Investment made by such fund may facilitate the commercialization within the organization of the innovative solution, and to speed up the development of the company.

Even if a start-up obtains financing for its early stage of development, the road to success is not easy. Experience has shown that the majority of new innovative companies that managed to gather financing in the early stages of development suffered a financial failure later on. The reasons for the failures differ, and in most cases start-ups fail to reach the expected financial goals as a combination of a few mistakes.

TP: » WHAT IF A START-UP DOESN'T MEET ONE OF THE AFOREMENTIONED CRITERIA?

JK: » In that case the chance of obtaining financing from that fund is rather faint. An important element is the structure of the fund's investment portfolio. If it features companies with similar solutions or from the same industry, the fund may be less likely to invest in a particular start-up. In the process of investment selection the fund is not only guided by its own investment strategy and start-up growth potential, but it also analyses other aspects of the company and its business in terms of the reality of business plans and risk. In the interest of the entrepreneur lies a cooperation with the fund, in which key people (partners, managers, investment managers) have experience in investment and management, a vast network of personal relations and a good reputation of active engagement in portfolio companies.

TP: » WHAT OTHER WAYS OF FINANCING DOES THE MARKET OFFER TO YOUNG ENTREPRENEURS?

JK: » Another way of obtaining capital for the development is *crowdfunding*. The aim in this case is to obtain the capital from a vast group of investors (private ones and, more and more often, institutional ones) through the mechanism of social networks. Special crowdfunding platforms are created to contact entrepreneurs with the community of potential investors.

TP: » OW DO THESE PLATFORMS WORK?

JK: » Investors put their money on projects that they find "interesting". Motivation of investors varies, from the desire to become a participant in a venture that is interesting from the investor's point of view, to the opportunity of being rewarded with a prize or recognition (e.g. being in the group of people who first receive the new product) or the desire of making a donation to the development of an interesting idea. Owners of such platforms earn money on fees from the gained capital.

TP: » WHAT SORT OF LEGAL REGULATIONS ARE IN POWER IN SUCH INITIATIVES?

JK: » To popularize crowdfunding, in 2012-2014 the US introduced legal acts (the so-called *JOBS act*) that allowed a major simplification of capital investments conducted through social networks, recognizing this mechanism of financing as an attractive way of financing small enterprises. There are already several crowdfunding platforms in Poland, however, as in many other European countries, no legal regulation simplifying this form of capital investment has yet been created.

TP: » WHAT DOES THE FUTURE DEVELOPMENT OF A START-UP THAT GAINED THE NECESSARY FUNDING LOOK LIKE?

JK: » Even if a start-up obtains financing for its early stage of development, the road to success is not easy. Experience has shown that the majority of new innovative companies that managed to gather financing in the early stages of development suffered from a financial failure later on. The reasons for failure differ (Figure No 2), and in most cases start-ups fail to reach the expected financial goals as a combination of a few mistakes. Success lies mostly in the hands of the start-up creators, and that's why entrepreneurs should prepare to handle their businesses single-handedly and an effectively manage dynamic growth.

KPMG'S TRAINING PROGRAMME

KPMG offers the creators of Polish start-upa special free training programme as a part of KPMG Start-up Academy. This program consists of a series of inspirational workshops that raise main business-related problems of companies in different phases of development, from the aspect of gaining financing, through managing dynamic growth (scale up), to the successful leaving of the owners from their well-developed company. More information can be found at kpmg.com/pl/startupacademy

Figure No 2

MAIN CAUSES OF START-UP FAILURE:

42%
LACK OF GENUINE DEMAND FOR THE PRODUCT OR SERVICE

29%
FINANCIAL RESOURCES INSUFFICIENT TO REACH BUSINESS GOALS OF THE START-UP

23%
LACK OF A PROPER TEAM

19%
MARKET DEFEAT WITH OTHER COMPETITORS

18%
TOO HIGH COSTS OF PURCHASE OF THE PRODUCT OR SERVICE OR AN INAPPROPRIATE PRICE STRATEGY

17%
PRODUCTS THAT FAIL TO MEET CUSTOMER'S EXPECTATIONS

WRONG BUSINESS MODEL THAT MAKES A SUCCESSFUL MONETIZATION OF PRODUCTS IMPOSSIBLE

14%
WRONGLY CONDUCTED MARKETING THAT MAKES IT IMPOSSIBLE TO REACH TARGET SEGMENTS OF CUSTOMERS

13%
LACK OF CUSTOMER FOCUS

TOO EARLY OR TOO LATE INTRODUCTION OF THE PRODUCT TO THE MARKET

LACK OF FOCUS ON THE KEY BUSINESS ASPECTS

INVESTOR-ENTREPRENEUR CONFLICTS

FINANCIAL REPORTING IN ACCORDANCE WITH THE STANDARDS

Financial reporting under International Financial Reporting Standards is a two-pronged challenge: on the one hand for the companies preparing such statements, and on the other hand – for their receivers.

Some of the accusations against financial reporting prepared in accordance with IFRS include, among others: extensive disclosure requirements (constantly expanding with new standards) and poor transparency or usefulness of information. This issue has been faced by both the International Accounting Standards Board (IASB) and the European Securities and Markets Authority (ESMA) in their ongoing work.

RELIABILITY AND TRANSPARENCY

One of the main principles of financial reporting is providing a true and fair view of an entity's position. This is possible through the application of proper accounting standards (principles) for the measurement and recognition of the effects of relevant transactions as well as ensuring adequate disclosures required by these standards. In case of financial reporting prepared in accordance with IFRS, the disclosure requirements are laid down in the respective standards. Such construction imposes an obligation on the entities to ensure that the requirements of all the applicable IFRS and IASB are complied with, which may in practice result in an increased volume of financial statements. This, however, reduces the usefulness and transparency of financial statements for their users. This observation has initiated IASB's work on the so-called Disclosure Initiative, which includes, among others, amendments to IAS 1 (Presentation of Financial Statements) and a planned review of the disclosure requirements in individual standards.

THE MATERIALITY CONCEPT

The revised IAS 1 emphasises the use of the materiality concept, not only in regard to the main parts of the financial statements, such as the statement of financial position or the statement of profit or loss and other comprehensive income, but also in terms of individual disclosure notes required by each applicable standard. In practice, this means that in accordance with the intentions of the authors of standards, when preparing explanatory notes, one should not automatically include every disclosure required by a particular standard, but only those that provide information relevant for the users of the financial statements. This, of course, requires judgement from preparers of financial statements. Additional rationale behind the above amendment is a comment expressed by the IASB stating that irrelevant information may sometimes obscure relevant information in the financial statements. It was also stressed that the line items indicated as required by IAS 1 (e.g. the required line items in the statement of financial position) may be additionally disaggregated in the main parts of the financial statements, if this leads to a more clear presentation of the financial situation. Finally, the provision of the standard which, according to IASB, had hitherto been interpreted as imposing a specific order of disclosures in the financial statements, have also been amended.

In accordance with the intentions of the authors of standards, when preparing explanatory notes, one should not automatically include every disclosure required by a particular standard, but only those that provide information relevant for the users of the financial statements.

AMENDMENTS – EXPLANATORY NATURE

Amendments to IAS 1 that have been in force since the beginning of 2016, at first glance do not seem to be extensive – the required scope of the financial statements, the preparation principles, the requirement to disclose the accounting policies applied, as well as including disclosures required by relevant standards have not changed. The changes are intended to explain IASB's intentions behind the existing principles of IAS 1 and IFRS as a financial reporting framework, and are effective for financial statements for periods beginning 1 January 2016 or later.

IMPROVEMENT IN THE QUALITY OF DISCLOSURES IN FINANCIAL STATEMENTS

In addition to the IASB's initiative, ESMA has also taken measures to improve the quality of financial statements that were reflected in a statement issued in 2015 on improving the quality of disclosures in financial statements (2015/ESMA/1609). This statement concerned, first and foremost, the problem of failing to adapt financial statements to the business nature of the entity preparing them, as well as the use of generic templates of financial statements and descriptions included therein. Attention was also brought to the lack of a critical approach in selecting notes due to focusing on only a formal compliance with the requirements of the standards – ensuring that all the required notes are included in the financial statements. In response to these observations, principles that should be considered when preparing annual reports were formulated in the statement: application of the materiality principle and continuous assessment of individual disclosures in this regard, improving readability of the financial statements (rearranging notes, brevity and consistency of information), presentation of relevant information in an accessible way for the users and tailoring the whole report to the nature of the entity (telling „your own story").

HOW TO PUT THE NEW PRINCIPLES INTO PRACTICE WHEN PREPARING FINANCIAL STATEMENTS?

First, it is worth to take a look at the existing financial statements and consider whether: the most important information is visible in them; disclosures are clear and do not contain irrelevant information; and the general message is consistent with other published information. After this analysis it should be considered whether and which notes can be removed from the financial statements due to their immaterial impact on the true and fair view of entity's position. Subsequently, the financial statements can be reorganized so that the most important notes from the point of view of the entity are placed at the beginning. Notes can also be arranged thematically, e.g. a group of notes related to fixed assets and their financing, working capital, management of liquidity, debt and equity, etc., instead of arranging them according to the order of items in the main statements. For improved readability, it is also worth to depart from placing a long description of applied significant accounting policies before all disclosure notes. It is more transparent to put a relevant extract from the accounting policy together with the relevant disclosure note (group of notes) and the disclosure of judgments applied in the measurement.

For improved readability, it is also worth to depart from placing a long description of applied significant accounting policies before all disclosure notes. It is more transparent to put a relevant extract from the accounting policy together with the relevant disclosure note (group of notes) and the disclosure of judgments applied in the measurement.

ACCOUNTING STANDARDS AND EVALUATION

One of the main principles of financial reporting is providing a true and fair view of an entity's position. This is possible through the application of proper accounting standards (principles) of for the measurement and recognition of the effects of relevant transactions as well as ensuring adequate disclosure required by these standards.

SUMMARY

The proposed changes require a considerable amount of work, however they will surely contribute to a reduction in the volume of the financial statements (financial statements of companies that have already adopted such changes have decreased by even a couple of dozen pages), and most of

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Monika has over 18 years of experience in audit of financial statements and accounting consultancy. She joined KPMG in 2005. Since 2012 she has been managing the accounting advisory services team, whose main tasks are related to advising clients on the impact of non-standard transactions on financial statements, implementation of International Financial Reporting Standards, in particular the new IFRS 15 (Revenue from Contracts with Customers) and IFRS 16 (Leases). Monika is a certified auditor.

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Marek started working at KPMG in 2006 in the financial services audit department. Afterwards he worked as a manager in financial reporting department within an insurance-financial services capital group in Poland. In 2016 Marek joined the accounting advisory services team where he deals with, among others, implementation of IFRS (including IFRS 15 - Revenue from Contracts with Customers and IFRS 16 - Leases), accounting for a non-standard transactions and restructuring within capital groups. He is a certified auditor and a member of ACCA.

Is it possible to achieve greater profits when trading partners increase their pressure on trading terms? Yes, and this is true not only in a situation when we decide to be deaf to the requests from the chains' buyers, but, above all, by improving the efficiency of the pricing management and commercial budgets as well as having an efficient and motivated sales team.

HOW CAN PRODUCERS GENERATE HIGHER PROFIT MARGINS?

The results of research and projects conducted by KPMG confirm that over 60% of companies can increase their profits by at least 5% thanks to a more efficient management of product prices. They also indicate that organizations which understand their product value and develop appropriate expertise in the scope of data analytics and pricing may have the chance to become leaders in their industry.

DIAGNOSIS OF THE SITUATION

When looking at the current situation on the Polish market, an affirmative answer to the question raised in the introduction may seem unrealistic. For several years there has been a regular price war between the players of the retail market, leading to a situation where the trade margins of retailers currently oscillate around a few percent, which in turn (together with an increase in labour costs) means that their business activity is on the break-even point.

KPMG's experience shows that it is possible to stop the erosion of trade margins. Although the process of changing trade policies is not easy, it allows a company to improve not only profitability itself, but also to gain a competitive advantage.

It is natural for retail chains to constantly raise expectations, e.g. increasing trade discounts for its suppliers, which causes a gradual decline in trade margins per unit of sales.
Of course, at first the producers would try to save their profit by reducing production costs, lowering advertising expenditures or seeking to optimize the cost of labour. However, based on market information, the source of improving profitability has already dried up. The only way to generate more profits seems to be an increase in sales volume and prices, which in turn inevitably leads to an increase in the investment level of distribution and promotion activities. Ultimately, it often turns out that the increase in sales volume unfortunately does not go hand in hand with the increase in the profit.

CAN THE QUESTION RAISED IN THE TITLE BE ANSWERED AFFIRMATIVELY?

KPMG's experience shows that it is possible to stop the erosion of trading margins. Although the process of changing trade policies is not easy, it allows a company to improve not only profitability itself, but also to gain a competitive advantage.

Efficiency of sales improvement through the continuous increase of discounts is limited, because successive cuts do not bring the expected results in the sales volume. Moreover, regular promotion is no longer attractive when compared with the ubiquitous offers such as „2 for 1" and implemented strategies – the so-called "dynamic pricing". Attaching an increasing importance to the proper pricing of goods and services is related to the fact that companies see in this area a great chance to improve operating results.

The focus should be placed on the following **3 basic areas**:
1 Pricing policy and efficient price management.
2 IImproving the efficiency of commercial budget management.
3 IImproving the qualifications and motivation of sales employees.

EFFICIENT POLICY AND PRICE MANAGEMENT

Research conducted by KPMG in global markets shows that over the past years only in 55% of all cases it was possible to achieve an increase in the revenue value after increasing prices. At the same time, this situation cannot be explained by the reaction to a direct reduction in the number of orders following the introduction of higher prices.

Low efficiency of pricing policies and, consequently, price management, primarily stem from the lack of understanding of its vision and principles among the members of an organization. In addition, the decisions regarding the increase itself are mainly based on profit requirements and intuition instead of market data. A very common mistake made by many organizations is a sudden decision to change price lists, without prior analysis of risk and contingency plans prepared to this end. As a result, what often occurs is that sales departments, on the one hand introduce new, higher prices, and on the other hand – in response to the market situation – effectively revert these price changes by increasing discounts and preserving the status quo when it comes to price.

Attaching an increasing importance to the proper pricing of goods and services is related to the fact that companies see in this area a great chance to improve operating results.

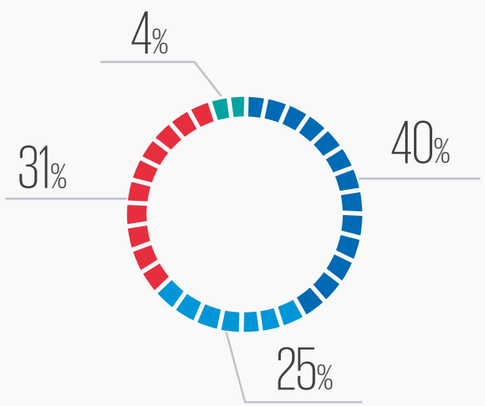
KPMG's analysis indicates that 70% of the senior executives of the surveyed companies believe that it is possible to improve the efficiency of pricing policies and treat them as one of the priority tasks.
A high potential to improve profitability that in turn contributes to the improvement of the current model of product pricing management, including increasing the efficiency of implementation of price increases, has also been confirmed.

[1] *„10% profit opportunity – pricing effectiveness and margin performance in the Australian market"*, KPMG Australia 2015.

[2] Spadek zamówień jako główny powód nieefektywnego wdrożenia podwyżek wskazało jedynie 15% respondentów, pozostałe 85% wskazywało inne przyczyny, m.in. obawę o spadek udziałów rynkowych lub utratę swojej dotychczasowej pozycji u partnerów handlowych.

Figure No 1

WHAT APPROACH IS USED IN YOUR COMPANY TO DETERMINE THE PRICE OF PRODUCTS?



- FOCUS ON COSTS (BASED ON COSTS PLUS MARGIN)
- FOCUS ON VALUE (BASED ON COMPREHENSION OF VALUE PROVIDED TO THE CUSTOMERS)
- FOCUS ON COMPETITION (BASED ON BENCHMARK PRICE)
- OTHER

Source: Report by KPMG International: "*The 10% profit opportunity*".

IMPROVEMENT OF COMMERCIAL BUDGET EFFICIENCY

Unfortunately, most companies carrying out regular promotional activities in organized trade and other distribution channels do not know their actual effectiveness. The prospects are not very optimistic – the projects and studies conducted by KPMG show that on average 2 in 3 promotions do not provide a return on the investment, and what is more, this trend is getting worse every year (in 2015 the effectiveness of promotional activities decreased by 3.1% compared with 2014).

A modular approach (Trade Funds Optimizer) developed by KPMG in Poland, based on own and other departments' experience, allows not only to assess and develop the effectiveness of individual arrays of promotional activities, but also to effectively implement them into everyday activities of commercial teams in the organization. Thanks to this approach and dedicated tools, people directly responsible for cooperation with clients, instead of habitually copy the same promotion plans every time, can focus their attention and resources on the most effective promotions. This allows to save some money for the promotion or to increase the sales value without using any additional investments.

It is necessary to have data on the effectiveness of individual promo and pricing activities, as well as their proper analysis. Moreover, a highly motivated sales team that – when supported by a proper analysis – can consciously fight not only for the volume but also the appropriate margin, is required.

[3] Source: KPMG Ireland/Nielsen Ireland

Figure No 2

TRADE FUNDS OPTIMIZER APPROACH HAS MANY STAGES AND ENDS WITH ANSWERS TO THE FOLLOWING QUESTIONS:

STAGE I – **TFM QUICK SCAN**: *SIZE* OF THE PRIZE, I.E. WHAT CHANCE DO I HAVE TO IMPROVE THE MARGINS?

STAGE II – **BLM BASELINE MODELING**: *EFFECTIVENESS MATRIX*, I.E. WHICH PROMOTIONAL ACTIVITIES ARE EFFECTIVE?

T&C MATRIX: *T&C HARMONIZATION* GAP, I.E. ARE MY TRADING CONDITIONS EFFECTIVE?

STAGE IV – **OPTIMIZATION FRAMEWORK**: *BLUE PRINT*, I.E. WHAT AND HOW SHOULD I IMPROVE IN COMMERCIAL BUDGET MANAGEMENT?

STAGE V – **ENABLERS DEVELOPMENT**: *TOOLS & IMPLEMENTATION ROADMAP*, I.E. WHAT ORGANIZATIONAL CHANGES AND TOOLS DO I NEED TO IMPLEMENT RECOMMENDATIONS OBTAINED IN STAGE III?

Figure No 3

FACTORS AFFECTING THE EFFICIENCY OF SALES TEAMS

- IN-DEPTH INTERVIEWS WITH FIELD EMPLOYEES
- INTERVIEWS WITH SENIOR MANAGEMENT EXECUTIVES
- PARTICIPANT OBSERVATION (EXECUTION OF TASKS, SEVERANCE PAY, SETTLEMENTS, ETC.)
- DOCUMENTATION ANALYSIS (PROCEDURES, INCENTIVE SCHEMES, REPORTS)
- REPORTING SYSTEM ANALYSIS AND SALES ANALYSIS

→ BUILDING INDEPENDENCE MAPS

→ INDICATING THE KEY FACTORS THAT HAVE AN INFLUENCE ON EFFECTIVENESS OF SALES TEAM

Source: KPMG in Poland, own work

MOTIVATING SALES EMPLOYEES

Unfortunately, even the most brilliant and profitable sales plans are of little help, if they are not properly enforced. Any organization with an extensive sales structure knows how difficult it is to change the behaviour of its employees. After all, it is salesmen who have influence on the perception of our organization among customers and their daily decisions have impact on the effectiveness of distribution systems - both in terms of numerical distribution and the cost of achieving it.
In most cases, only some elements of systems for management and motivating the employees need to be improved in order to achieve significant change in the behaviour of salesmen. Most frequently, the most essential points include quality of goals' communication and monitoring or maintaining the balance between rewarding individual and team achievements. Just as there are no two identical sales teams, there are no universal solutions that can be effectively applied to any sales organization. Therefore, each sales department should be treated individually and holistically – on the one hand by looking for areas whose change will bring the best results for the entire organization, and on the other, by looking for „change agents" within the organization who, by setting an example, will help bring entire teams to higher levels of efficiency.

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Jan specializes in enterprise management consulting. He is experienced in, among others, market strategy consulting, restructuring, estimating market and investment potential, process improvements and designing organisational structures. Jan joined KPMG in 2006 and since then has been providing services for entities from telecommunications, energy, production and financial industries.

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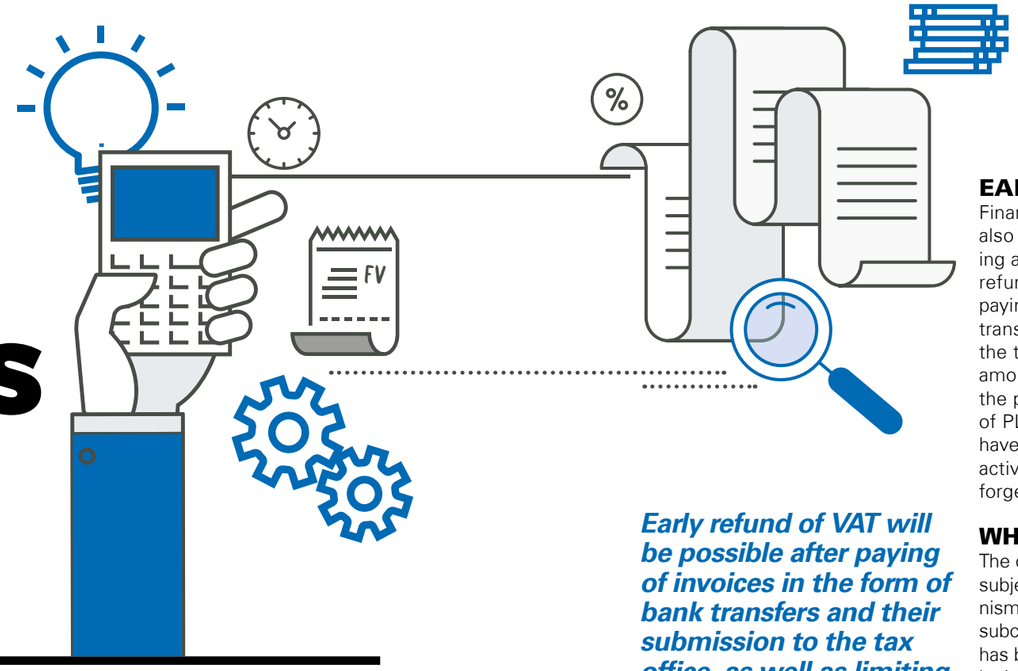
CHANGES TO VAT REGULATIONS in 2017



Taxpayers have already become accustomed to frequent changes in tax regulations. This particularly affects VAT regulations which are amended even during the fiscal year. The new year 2017 has brought further changes that are effective from 1 January.

In principle, the changes should reduce the occurrence of „carousel frauds" and frauds on VAT returns. However, it appears that the amendments to the regulations will affect practically all VAT taxpayers in our country.

NEW SANCTIONS

The most important change is the return of additional tax liability (30% sanctions) for the understatement of tax liability amount or the amount of tax to be refunded to the Polish VAT system. The regulation abolished in 2008 (and then found to be in compliance with the Community rules by the ECJ) is applicable for settlements from 1 January 2017. Additional liability may be reduced to 20% if the taxpayer, after the control proceedings (or during the audit procedure), makes a self-correction in a VAT return and pays liability in the correct amount together with interest (pays back the improperly obtained tax refund). Exemption from the sanction is limited to only clerical errors and obvious mistakes or those affecting the proper settlement period as well as situations when the taxpayer had made an appropriate adjustment and settled the liability together with interest prior to the initiation of control. Therefore, in practice, any error identified by the tax authorities (treasury authorities) will result in a sanction of at least 20%.

It is important to note that the amended provisions also introduce a completely new sanction in the amount of 100% of the accrued tax resulting from the issuance of the so-called „blank invoices" which were used for the understatement of liabilities or overstatement of the amount to be returned.

QUARTERLY AND ELECTRONIC RETURNS

The restriction to submit VAT returns on a quarterly basis will apply only to small taxpayers within the meaning of the Act who have been conducting their business activities for less than a year. All other taxpayers who have previously submitted the quarterly return, will therefore have to return to monthly settlements, starting from January 2017.

EARLY TAX REFUND

Financial liquidity of taxpayers will also be affected by changes regarding an early 25-day VAT refund. Early refund of VAT will be possible after paying of invoices in the form of bank transfers and their submission to the tax office as well as limiting the amount arising from the transfer from the previous returns to the low level of PLN 3 000. The taxpayers who have been conducting their business activities for less than a year can forget about an early refund.

Early refund of VAT will be possible after paying of invoices in the form of bank transfers and their submission to the tax office, as well as limiting the amount arising from the transfer from the previous returns to the low level of PLN 3 000.

In addition, most companies will now be required to submit VAT returns only in an electronic form (this obligation applies to all companies which are involved in intra-Union trade, perform deliveries subject to the reverse charge mechanism in the country or electronically submit income tax returns). It should be noted that non-submission of VAT returns in the electronic form will trigger sanctions listed in the Fiscal Penal Code. Many taxpayers have already been submitting electronic VAT returns, but in practice the change in the form of communication with the tax office can be challenging for foreign entities registered for VAT purposes in Poland. By extending the obligation of submitting a monthly VAT returns in the form of a Standard Audit File-Tax from 2017 to medium and small taxpayers, the tax authorities potentially gain vast possibilities to quickly verify the accuracy of taxpayers' VAT returns.

WHAT ELSE IS CHANGING?

The construction sector expects to be subject to the reverse charge mechanism in case of services performed by subcontractors. Although the scope has been specifically defined by the legislator in the new Annex No 14 to the Act, the lack of a legal definition of a subcontractor will certainly arouse many doubts in the case of settlements concluded by construction companies. The fight against frauds will also be supported by the possibility to refuse to register new taxpayers, if there exists a suspicion that they have provided false information in the VAT return or when it is impossible to contact them or their proxy. In case of the registration of a new taxpayer, the proxy who has represented the entity during the registration processes will be jointly liable for 6 months for the taxpayers' liability amounting to PLN 500 000. The tax authorities will also obtain a tool to deregister the taxpayer, especially in the case of issuance of blank invoices or participation in a VAT fraud.

This time the amendment to the VAT Act will be of a particularly wide scope. The introduction of the procedures verifying the correctness of VAT returns should be included among the priorities of every CFO and chief accountant. Additional tax liabilities (including those amounting to 20%) will not be a welcomed outcome of possible mistakes.

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THE NATURE OF VALUATION OF SMALL AND MEDIUM SIZED ENTERPRISES

Small is beautiful, but… not always easy to value. Contrary to many opinions, valuation of small and medium-sized enterprises („SMEs") is often not only more difficult than valuation of large companies, but also requires more work from the valuator due to the necessity of taking into account the specific issues arising from the nature of these kind of companies.

When starting the SME valuation, in addition to understanding the environment in which the company operates, including, among others, prospects arising from the market situation, one should also examine in detail the issues related to the direct participation of the owners in the management of the company. These may include the level of dependence between the company's success and the presence of the owner at the company, settlements with him and his relatives, or private assets included in the company's balance sheet. One should also consider the aspects arising directly from the specific business activities of SMEs, including additional risks and limitations related to, among others, the size of the valuated entities or their dependence on key partners, which should be properly taken into account when estimating the value.

FACTORS RESULTING FROM THE OWNER'S POSITION AND HIS ROLE IN A COMPANY

In the case of SMEs, unlike large and developed companies, the company's management board very often consists of the company's owners or people who are directly dependent to them. Thus, the owners exercise influence over the company's business activity and so constitute an essential factor for success with their contacts, as well as personal involvement in the company. Due to their dual role (owner/management board) the personal interest of the company's owner is usually in line with those of the company itself. This often leads to a situation in which the boundary between the assets and costs of the company and those of its owner's becomes more vague.

Since there are many similar examples, when starting the valuation of a company, appropriate adjustments should be made in such a way that the company's assets, its performance and generated cash flows only include the items that are related to the company's business activity, and their value reflects market levels. This type of standardization is essential for a proper determination of current and anticipated financial situation of the company that constitutes the basis for valuation.

These adjustments are necessary in order to determine the fair value of the company's shares. In accordance with the International Financial Reporting Standard 13 (IFRS 13) the fair value is defined as „the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date" – hence, it is necessary to adopt the perspective of a market participant.

This is also important in the context of the owner's role in the company's current business activity – in particular, the extent to which the position and performance of the company depends on the owner's presence in the company. In the case of SMEs, it's often the case that the total revenues generated by the company (or their significant part) depend on the owner's personal relationships with key customers, or his/her knowledge, experience or skills. This may lead to a situation where, the disposal of the company and the termination of the owner's involvement in the company operations results in a significant collapse in company revenues, causing a decrease in the company value. Therefore, prior to the valuation, it is of key importance to determine what role the owner/management board plays in business activities, in particular, to what extent the results of the company depend on the presence of the owner.

THE EFFECTS OF LACK OF DISTINCTION BETWEEN THE COMPANY AND THE OWNER'S ASSETS AND EXPENSES:

1. Including the owner's private assets on the company's balance sheet – in extreme situations the company may be the „owner" of private cars or real estate, which are not related to its business activities;
2. Settlements in the form of loans and guarantees between the company and the owner, whose terms may be adjusted depending on the needs of the owner;
3. Overestimating or underestimating the company's operating expenses e.g. by recognizing the owner's private costs or non-market levels of remuneration settlements concerning work performed for the company by the owner or his family (e.g. paying monthly salary to the relatives of the owner, even if they are not only not involved in the activities of the company, but also when they do not even set foot in the company

FACTORS RESULTING FROM THE NATURE OF THE COMPANY

Financial data of companies from the SME sector, which constitutes a basis for their valuation, can be of varying quality – which is true in particular for financial plans. This is due to the fact that in the case of small companies, the process of planning and budgeting is often superficial, insufficiently documented or does not exist at all. Historical financial data may be inconsistent or complied with undue care. Our experience also shows that financial statements are often not subject to auditors' examination.

The concerns may also be risen by the reasonability of the forecasts. Due to a flexible approach to the planning process – forecasts prepared for the same date and for the same company may differ significantly from each other depending on the purpose for which they were prepared. For example, in a situation where the forecasts are developed in order to sell a company, its owners tend to overestimate the company's ability to generate cash flow in order to maximize proceeds from the sale. On the other hand – in the case of optimization of the structure, owners may want to underestimate the value of company by minimizing the costs associated with the planned transaction.

ANALYSIS OF THE COMPANY GROWTH DYNAMICS

Prior to the valuation, the forecasts for the company should be precisely analysed in the context of the company's financial history and the independent analysis of the development of the market on which the company operates. Our experience shows the elements which should be specifically considered include:

1. **HIGH DYNAMICS OF REVENUE GROWTH DURING THE FORCASTED PERIOD – it is often difficult to support it, especially when taking into account the recent company's history or the anticipated market growth rate;**
2. **INCREASE IN OPERATING MARGIN – when planning to increase revenue, owners very often underestimate costs necessary to incur to achieve the expected growths; furthermore, planning is very often done in isolation from market changes concerning e.g. increase in commodity prices and employees' pressure on the salary increase;**
3. **NVESTMENT EXPENDITURES – owners very often not only do not consider the necessity to recover the existing fixed assets that had been worn out over time, but also do not take into account the expenditures required to be incurred in connection with the planned revenue growth;**
4. **BUSINESS GROWTH AFTER THE PERIOD OF DETAILED FORECAST – owners who got used to high dynamics of their business growth, assume that their business will be growing at the same pace all the time, without being aware that continuous dynamics of the revenue growth may not be achievable after reaching the certain stage of development of the company.**

In order to identify and normalize (verify) financial forecasts, it may be useful to analyse the historical dynamics of the company's development, the degree of budgets realizations, development of the company as compared to its competitors and the prospects for changes in key determinants of company's profitability in the future.

FACTORS RESULTING FROM THE VALUATION METHODOLOGY

Assuming that a company continues its business activity in the future, the company value results directly from future cash flows that the company generates for its owners. The most common approach used to estimate the fair value of the company shares is the income approach – discounted cash flow method (DCF). It allows to impose necessary adjustments, which result from the previously discussed nature of SME, and include specific risk factors during the forecast period. Other valuation methods, such as: the multiples of comparable listed companies depend largely on comparability, which in the case of SME is subject to special restrictions.

Due to the nature of companies, the form and scope of the business activity of SMEs may considerably differ from large companies, which makes identification of companies compared to the valuated SMEs very difficult or even impossible – especially without an access to relevant databases and publications. Furthermore, given the scale of business activity, its area, the degree of development and the level of profitability, the multiples of the comparable listed companies may require additional adjustments that (unsupported by analyses used by specialized valuation teams of international advisory firms) are often discretionary.

The situation is similar with transaction multiples. In this case, the uniqueness of transaction conditions, which are often not available to the public, may create an additional problem. These conditions relate to, among others, forms of payment (cash, stocks, etc.), the date of payment (immediate, deferred, or subject to certain conditions) and additional arrangements (e.g. the repurchase of a part of the sold entity).
A separate issue is the selection of appropriate multiples and the use of financial results of the company to calculate its value. In the case of the most commonly used EV/EBITDA multiple (enterprise value to operating profit plus amortization), it is of key importance (except the abovementioned issues) to normalize the company's EBITDA, which – in the case of SMEs – may be a complicated process that should include, in particular, the elimination of all non-market and one-off costs and

Figure No 1

Due to a flexible approach to the planning process – forecasts prepared for the same date and for the same company may differ significantly from each other depending on the purpose for which they were prepared for. For example, in a situation where forecasts are developed in order to sell a company, its owners tend to overestimate the company's ability to generate cash flows in order to maximize proceeds from the sale.

revenues, which the company will not be able to repeat in the future. Such items may include all private costs and revenues of the owner (referred to above), but also, for example, received subsidies, paid compensation, one-off agreements, bargains purchases of commodities etc.

The multiples method is therefore used as a complementary method for the income approach – as a confirmation of reasonability of the final valuation result. A key condition for the application of the DCF method, under the income approach, is the availability of the company's financial forecasts allowing the calculation of cash flows, which will then be discounted on the valuation date with the appropriate discount rate. Depending on the practice, the discount rate may include appropriate adjustments intended to reflect the risks associated with the occurrence of cash flows. In the case of SMEs, the most common adjustment is a size premium. Its application allows to include the risk associated with the size of SMEs in a discount rate – as compared to the companies constituting the basis for calculating the cost of capital. The basis for the application of such a premium is the assumption that smaller companies are characterized by much higher volatility than larger entities, and thus, the risk associated with the return on investment in these entities is higher than investments in larger companies.

When calculating the discount rate, attention should be paid to a number of issues specific for SMEs whose occurrence may increase the risk of achieving forecasted cash flows. These may include, among others, risks associated with excessive concentration – dependence of the company on one or a group of suppliers and/or receivers – or dependence of the company's results on key personnel.

SUMMARY

Valuation of small and medium-sized enterprises, seemingly simpler than analyses of large companies, may often prove to be much more complicated and time-consuming – it requires extensive experience and taking into account many complex factors. The above list of issues requiring attention serves only as an example, since, in practice, their number can be unlimited.

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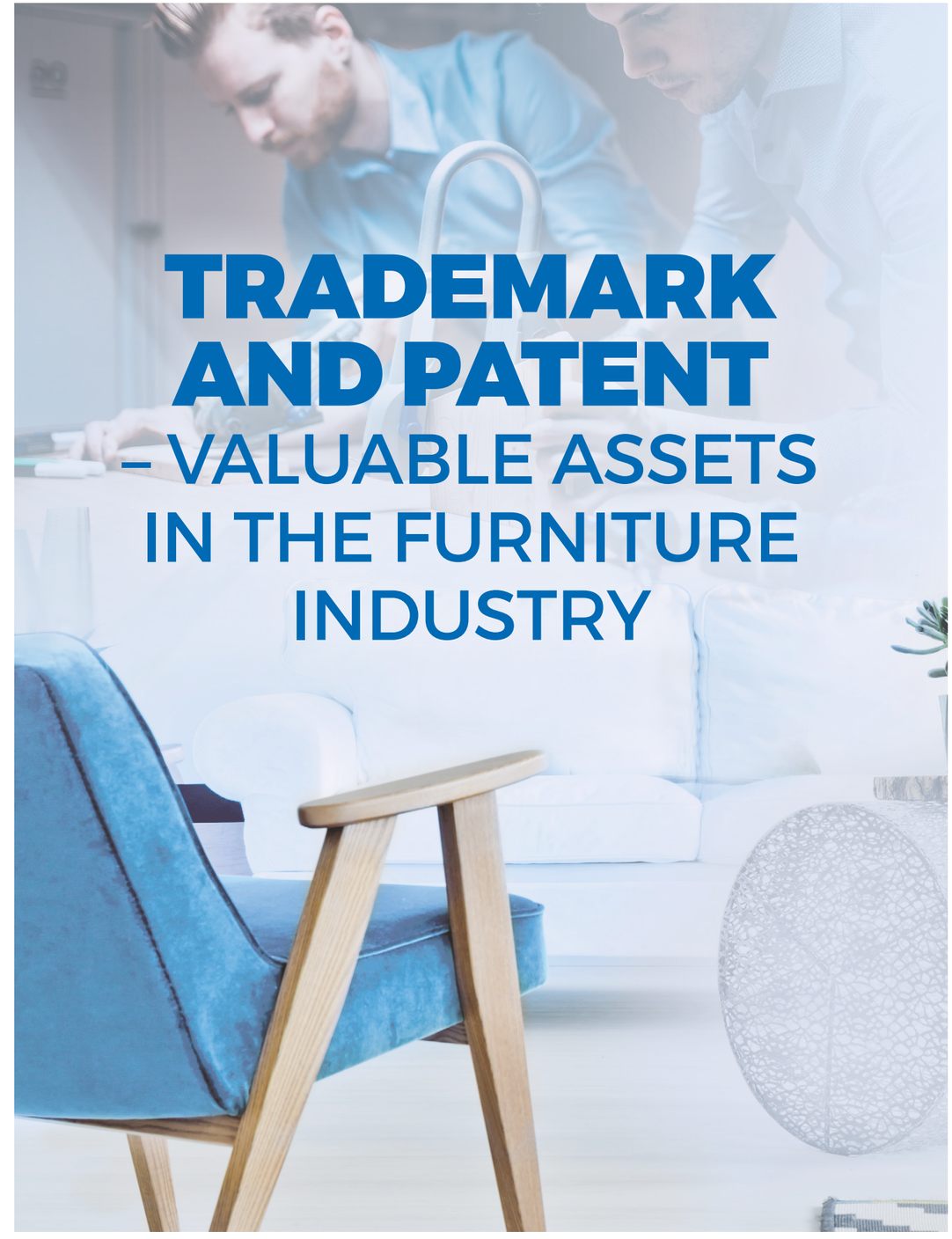
IN THIS ISSUE



TRADEMARK AND PATENT – VALUABLE ASSETS IN THE FURNITURE INDUSTRY

Polish furniture companies have been strengthening their position in Europe year by year. According to the analysis by the Polish Chamber of Furniture Manufacturers, the export of furniture in 2016 may exceed PLN 41 billion. The majority of the furniture goes to Germany, Great Britain and Czech Republic. Polish furniture is purchased not only in Europe, but also in countries such as Brazil and the Arab Emirates. It is also gaining popularity in the US, Romania and Slovakia. The Chinese and the Iranian markets are also opening up to Polish exporters.

Polish furniture manufacturers continuously invest in new machines to improve efficiency. Consequently, their products are absolutely world class level as far as quality and design are concerned. In the last 25 years the industry has achieved a huge technological success. Big European chains have started to purchase furniture in our country, and experts are saying that this tendency will continue. The time has come for Polish manufacturers to face new challenges, such as creating their own brands and patent protection of their own technical developments.

IT'S TIME FOR YOUR OWN BRANDS

It is estimated that if Polish manufacturers exported goods only under their own brands, the value of the furniture sold abroad could reach between PLN 50 and 60 billion annually. Although Poland is a furniture superpower, our brands don't receive recognition abroad. Only a handful of companies sell their products under their own logos. Many Polish manufacturers produce furniture for their foreign partners who later sell them under their own brands.

CREATING YOUR OWN BRANDS

It is a business challenge that requires ensuring appropriate legal protection. Apart from the trademark, protection can also encompass unique technical solutions.

TRADEMARK REGISTRATION AND PATENT PROTECTION

Technological solutions used in furniture industry are protected under the industrial property right as the so-called ‚utility models'. Thanks to them the company that developed a certain utility model can ensure legal protection guaranteeing them exclusivity for using it and preventing its innovative solutions from being copied by competitors.

In some cases, innovative solutions applied in manufacturing furniture or used in the furniture itself may be subject to patent protection. Patents are granted in all areas of technology to inventions that are new, worldwide, have a standard of invention (are unobvious) and show a possible industrial application.

If a producer wants to get a protection abroad, they have to follow the appropriate national or international route (e.g. European route, European patent). The aforementioned laws, being property laws, are a part of the company and have an economic value that influences the value of the whole company.

Property laws, such as trademarks, patents and protection rights of utility models, apart from strengthening the position of the entrepreneur, can also be a valuable asset. They increase the carrying value and present the real value of the company. They can also be a tax asset and contribute to lowering the tax burden.

INTERNATIONAL EXPORT EXPANSION AND THE LOCATION OF THE FOREIGN COMPANIES

When planning export expansion on certain markets, entrepreneurs need to make decisions concerning the location of sales offices, the centres of intellectual property and international e-commerce. Is it worth to open a sales centre in the UAE, if you are planning expansion to the Far and Middle East markets? Is Switzerland, a popular location for many intellectual property centres, really the best choice for each and every furniture manufacturer? There is no clear answer to these questions. To make the right choice without risking that costs will minimize benefits, final decisions should be preceded by the analysis of the overall business and investment plans, cash flow, future investment or consumption goals, as well as the analysis of the extent to which property laws like trademarks or patents can be used.

It is estimated that if Polish manufacturers only exported goods under their own brands, the value of the furniture sold abroad could reach between PLN 50 and 60 billion annually.

THE USE OF TRADEMARKS AND PATENTS IN TAX PLANNING.

Property laws, such as trademarks, patents and protection rights of utility models, apart from strengthening the position of the entrepreneur, can also be a valuable asset. They increase the carrying value and present the real value of the company. They can also be a tax asset and contribute to lowering the tax burden.

PROPERTY RIGHTS

Legally protected property rights constitute intangible assets that can be subject to tax depreciation, provided that we properly plan which of the companies from the group will hold these rights and in what way and under what sort of agreements other companies from the group benefit from protecting these rights. Subjective rights are an important tool of tax planning, and should thus be used in a way that increases tax effectiveness.

When conducting structural changes, it is worth preparing the family business for the next generation of owners and maintain tax neutrality. A proper model of using trademarks is also important from the perspective of the VAT tax. Depending on the way the trademarks are used we may apply VAT-neutral ways of using and transferring patents and trademarks without the risk of any claims.

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RESTRUCTURING – A WAY TO REDUCE DEBT

From 1 January 2016 entrepreneurs in a state of insolvency or at risk thereof may make use of four types of restructuring proceedings. The simplest of them is the arrangement approval proceeding, which makes it possible to conclude an arrangement with creditors in a non-formalized way and without losing the right to manage the company.

An arrangement, after the fulfilment of certain conditions, in particular after approval by the court, will bind all creditors who are subject to it. The proceeding for the arrangement approval is intended for entrepreneurs who are at risk of insolvency and – in order to avoid bankruptcy – asses that they have the ability to gain acceptance for the restructuring proposals of the majority of creditors (representing 2/3 of the aggregated value of the debts).

WHAT ARE THE BENEFITS OF AN ARRANGEMENT CONCLUDED DURING APPROVAL PROCEEDINGS IN COMPARISON TO INDIVIDUAL DEBT REDUCTION?

An arrangement approved by the majority and concluded during approval proceedings is binding on all creditors, even if they voted against the proposal. In case of individual negotiations, a creditor who has not agreed to the proposal, will not be subject to it. Therefore, an entrepreneur, when carrying out restructuring proceedings for an arrangement approval, is more likely to achieve the expected result.

A LICENSED SUPERVISOR

An arrangement supervisor, mandatorily appointed during the arrangement approval proceedings (a licensed restructuring advisor or a restructuring advisory company), is obliged to verify the documents and information provided by the entrepreneur. Thanks to him, creditors gain full access to information on the arrangement proposals, which simultaneously become more reliable for them. The amount of the liabilities redeemed in restructuring proceedings, including the arrangement approval proceeding, does not constitute an entrepreneur's income within the meaning of the Corporate Income Tax Act (Article 12 (4) (8b)) and the Personal Income Tax Act (Article 14 (3) (6)), whereas in the case of redemption carried out in individual negotiations, the redemption amount will increase the tax base.

HOW TO CONCLUDE AN ARRANGEMENT?

1. Choosing the arrangement supervisor

When at risk of insolvency, the entrepreneur should choose an arrangement supervisor, who can be a licensed restructuring adviser or a restructuring advisory company, and conclude with this entity an agreement specifying the responsibilities of the arrangement supervisor, minimum range of which is described below, as well as his salary.

2. Determining the arrangement date

The entrepreneur should determine the arrangement date not earlier than three months before the date of submission of the arrangement approval application. The creditors' rights to vote on the arrangement and the consequences of its approval are defined at the arrangement date.

3. Restructuring plan and arrangement proposals

The arrangement supervisor, based on information received from the entrepreneur, draws up a restructuring plan and together with the entrepreneur prepares arrangement proposals, which should specify the method of restructuring the entrepreneur's liabilities, e.g. by postponing their execution, payment in instalments, reducing the amount of liabilities, converting them into shares or stocks, amending or waiving securing rights or repaying the liabilities from the company's profit.

4. Report on the possibility of arrangement implementation

The arrangement supervisor draws up a list of all the entrepreneur's liabilities and their disputed obligations. Based on the above preparatory procedures, the arrangement supervisor should prepare a report on the possibility of arrangement implementation by the entrepreneur.

5. Collecting votes

After determining the arrangement date, the debtor, with the help of the arrangement supervisor presents creditors with voting cards and collects votes expressed in writing. The role of the arrangement supervisor is to provide on the request of the creditor information on the financial situation of the entrepreneur and the possibility of arrangement implementation in order to make a decision.

6. Adoption of the arrangement

The arrangement is adopted if the majority of votes of all creditors is obtained (not only those who have voted), representing at least 2/3 of the total value of all liabilities. Disputed claims of the entrepreneur cannot exceed 15 % of total claims. The adopted arrangement is subject to approval by the court within two weeks from the date of submission of the proposal.

The arrangement approval proceeding is a very interesting legal instrument and its introduction should be assessed positively. The legislator should also grant the entrepreneurs adopting this procedure the possibility to obtain a suspension of any individual enforcement proceedings for a limited time, in order to allow them to negotiate with creditors.

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IN THIS ISSUE

GDPR – WHAT'S NEW

It's hard to overstate the role of a consultant (or a lawyer) in the preparatory process for the new EU directives concerning the General Data Protection Regulation. On 25 May 2018, both personal data controllers and processors (to whom GDPR's broader territorial scope applies) will have to prove full compliance to the new regulations.

Currently the processing of personal data is regulated by the Act of 29 August 1997 on the Protection of Personal Data, which introduced the Directive 95/46/WE. These regulations will remain in force for a maximum of a year and a half.

NEW REGULATIONS: LEGAL BASIS

Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) shall apply from 25 May 2018.

There are areas, such as the new responsibilities regarding personal data security, that will strongly affect the business and its costs. Even though the EU reform is not a complete revolution, both controllers and processors are aware of the new dimension of liability for non-compliance to the new regulations.

FINES FOR NON-COMPLIANCE

GPDR regulates strict administrative fines for infringements of up to 10 000 000 - 20 000 000 million EUR, or 2-4% of the total worldwide annual turnover (in the case of an undertaking). There may be further fines or penalties added on a national legislative level. For some entities such fines, if imposed, could mean the end of their business.

New regulations concerning personal data protection include not only the GDPR, but also national regulations that are currently being prepared, providing further details on some of the issues (such as a legal basis for processing data in compliance with the legal obligation or the performance of a task carried out in public interest, or the conditions of processing biometric data), modifying GDPR regulations (e.g. minor's age of consent for personal data processing), or limiting or excluding the use of GDPR (the scope of the obligations and rights of the data subject). There are also the European Commission directives, those of the Article 29 Working Party (future European Data Protection Board), and others, such as good industry practices regarding the security of personal data processing.

Legal approach to the new topic (interpreting the provisions), general knowledge of the law (not just regarding the GDPR), proximity to the sources of legal information (e.g. about legislative work), and industry expertise may prove indispensable in the process of adjustment to the GDPR.

WHEN IS A CONSULTANT NEEDED?

In some areas the concept of personal data protection in line with the GDPR remains unchanged (for example, the principles apply to any kind of processing of a natural person's personal data).

However, there are areas such as new responsibilities concerning the security of personal data (i.e. a data protection impact assessment), that will strongly affect business, also from the costs perspective. While the EU reform is not a complete revolution, both controllers and processors (data processing entities) are aware of the new dimension of liability for non-compliance with the new regulations. Considering the numerous sources of these regulations, waiting until 24 May 2018 without taking any action is simply not an option for controllers and processors.

HELPING IMPLEMENT NEW REGULATIONS

Some controllers and processors are already embracing the change, while others are only starting to prepare. To reach full readiness and compliance, controllers and processors will require a team of key experts. They will definitely be responsible for managing given units, like current Information Security Administrators (ISA) or their unofficial counterparts, IT systems administrators, or IT specialists and persons overseeing particular departments (sales, marketing, customer service, finance, HR, etc.). Consultants or even teams of consultants specializing in personal data protection will also be indispensable due to novel legal matter and the aforementioned risk of fines.

WHO NEEDS CONSULTANT'S SUPPORT?

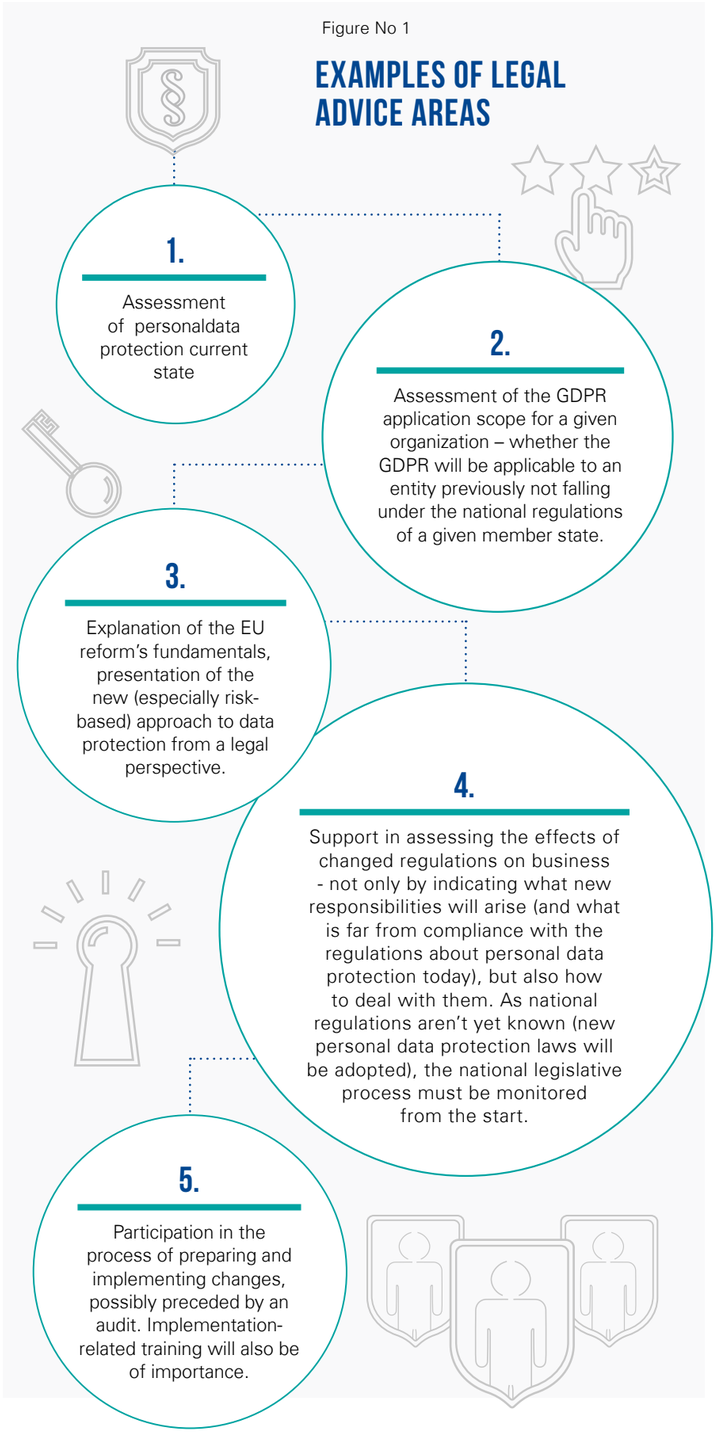
A consultant specialist will support controllers and processors to whom GDPR applies. From an organization's perspective the consultant can serve management (by explaining the principles of liability), ISA and ITSA alike. Support departments such as IT, compliance, HR or each business division - sales, customer service, etc. - also have a part to play. At first, a lawyer has to inspire and provide knowledge. Knowledge is the keystone for each participant's role. A CIO won't be able to do much if they're not familiar with the blueprint of Internet sales, and a sales manager needs to know the purchasing structure to which they then adjust their actions. If the GDPR assumes as crucial the privacy by design premise and its constituent privacy by default, a central decision-maker must be chosen to evaluate and configure all actions according to their compliance to personal data protection standards set out by pertinent laws. A consultant can use their knowledge to fulfill such a role.

As is the case with any new legal regulations, a lawyer's engagement during the adjustment process seems only natural. Next year and a half are going to be full of work, not just for controllers and processors, but consultants as well.

WHAT'S NEXT?

The work of a consultant (also a lawyer) will not be over on May 24 2018 - adherence to the GDPR, and the approach agreed upon during the preparatory period, controllers' or processors' practices will be verified by supervisory authorities (one-stop shops), the European Commission or European Data Protection Board. Their assessment may lead to further guidelines. Lawyers may also prove indispensable when dealing with infringements of data subject rights and infringement claims, or representing an organization before supervisory authorities.

Figure No 1



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IT DIRECTORS LEADERS OF DIGITAL TRANSFORMATION

The rapid development of technology we are witnessing at the moment has major influence on the way companies function. Numerous possibilities appear due to the popularity of mobile solutions and new technologies like cloud services, advanced analytics, and cognitive computing (new architecture of computing systems capable of "learning") provide many possibilities for a lot of companies.

Research shows that 27% of disruption is down to new digital innovations in product/service delivery, and 23% is down to new forms of customer engagement

DIGITAL STRATEGY FOR COMPANIES

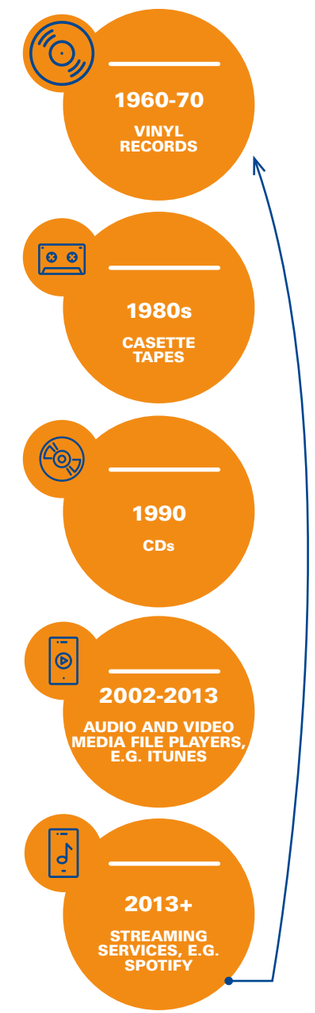
Management boards see the use of cutting-edge IT solutions as a tool for development and gaining competitive advantage, especially now, during the fourth industrial revolution. At the same time, management boards are aware that forfeiting change in this field can have serious consequences. This is the reason why more and more companies are developing a digital strategy – over 35% of companies already have an enterprise-wide digital strategy. Most often the management board is the 'owner' of the digital strategy. However, in Poland and other countries of Middle and Eastern Europe digital strategy is often in the hands of IT divisions.

PROSPECTIVE CHANGES

A changing environment and digitally aware customers require that today's business is fast and flexible. Business itself is better informed about new technologies, and is capable of developing its own solutions, thereby entering the domain previously reserved exclusively for IT divisions. Availability of new technologies, numerous possibilities for acquiring modern solutions, and stakeholders well versed in the digital – all this heralds great changes in the functioning of nearly all organizations, and runs the risk of IT departments being sidelined.

Figure No 1

MUSIC INDUSTRY THE PERFECT EXAMPLE OF DIGITAL DISRAPTION "RETURN TO THE PAST"



EVERY DIGITAL DISRUPTION CHANGES THE EXISTING ORDER, CREATES NEW WINNERS, AND LEAVES BEHIND THOSE WHO CANNOT ADAPT FAST ENOUGH

WHAT DO DEVELOPMENTAL CHANGES MEAN TO IT MANAGEMENT?

Findings of the global Harvey Nash / KPMG CIO survey conducted in 2016 in 82 countries including Poland, demonstrate beyond doubt that according to the majority of CIOs it's not enough for the IT department to merely support business anymore. Business has become an aware and very demanding customer. What is expected of the IT department is no longer simple maintenance of systems, but also innovation, playing an active part in creating and implementing innovative ideas. Efficiency and flexibility that allow turning innovative ideas into products and services are becoming the measure of company's success.

Flexible and efficient action requires the cooperation of IT and business which is why 'better engagement with customer' is currently the main goal of CIOs. It is one of the most important CIO priorities globally, and has increased in importance in the last 3 years.

IT managers are aware that their part in organizations is undergoing a big change. Knowledge and experience they have acquired thus far allow them to act in an unprecedented way, clearly aimed at business (four in ten CIOs now spend at least one day per week outside IT). New tasks don't take away the responsibility to provide the highest quality service for business on a daily basis. The main task of CIOs is providing technology that allows for an efficient execution of current operations. Only by fulfilling that requirement will IT leaders be able to take a step towards the position of a technology expert, strategic partner of the board, and a leader of digital transformation. Last year's CIO survey shows that 55% of IT leaders believe that in the next 5 years their career will develop outside of IT, while 23% claim that changing their role, they will join executive board, who need their digital skills more than ever before.

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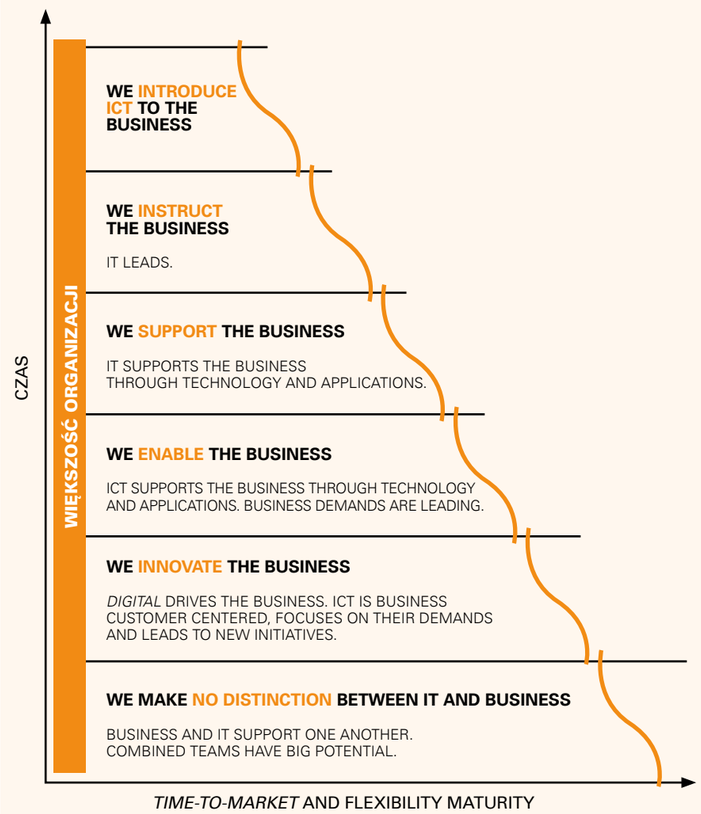
Figure No 2

DIGITAL DISRUPTION PUSHES ORGANIZATIONS TO TRANSFORM IT ROLE



NEW EXPECTATIONS

Engineering and programming skills are no longer sufficient for CIOs, who are required to have an in-depth knowledge of the business, management and controlling. Many of them add soft skills to improve their engagement with the business and speak the language of business requirements and benefits. This change affects not only IT leaders, but the whole field of IT. It requires reorganizing both IT departments and business, which leads to increased cooperation efficiency and opening up to new options made possible by the development of technology. IT managers face new challenges that require a shift from operational to creative thinking.

READ THE NEXT ISSUE OF 'TURNING POINT' AND LEARN ABOUT GLOBAL TRENDS AND DIRECTION OF CHANGES IN MODERN IT DEPARTMENT ORGANIZATION.

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