Analyst Insight

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The CIO's Role in Indirect Tax Compliance: Deploying Solutions on Spec and on Budget

With many governments across the world facing revenue deficits, countries are continuing to accelerate their indirect tax audit initiatives with companies operating in their respective jurisdictions. The objective is simple: find as many companies in violation of indirect tax compliance as possible to make up for the revenue shortfall. That said, companies are paying closer attention to proper indirect tax preparation, filing, and remittance / recovery than ever before. As a result, they are looking at streamlining these processes through the help of technology. These organizations are facing an interesting dilemma: tax managers are in charge of compliance, but the implementation of technology used to drive compliance is in the hands of Information Technology (IT) managers. An IT executive's performance evaluation is often project-based: how to implement a solution on time and on budget is the primary objective, while the solution's business alignment and impact often becomes secondary (or "lost" in intangible terms, often requiring the justification of business-line managers to address its effectiveness). Nonetheless, while the entire company may not be involved in indirect tax management, the repercussions of non-compliance impacts everyone: an increase of unforeseen cost and liability that damages the business and impacts profitability. As such, Chief Information Officers (CIOs) should continue to work closely with tax departments to ensure solution alignment to compliance initiatives.

Analyst Insight

Aberdeen's Insights provide the analyst perspective of the research as drawn from an aggregated view of the research surveys, interviews, and data analysis

Technology-Driven Compliance

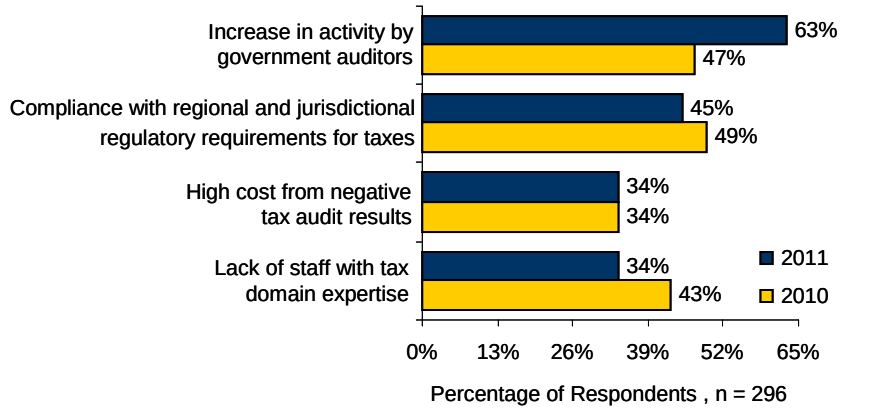
CIOs are aware that custom software development and integration costs run higher than typical off-the-shelf software. It is with this hurdle in mind that they undergo a stringent source-selection process. Thus best-of-breed tax solutions are evaluated for their ease of integration with existing enterprise applications, such as their Enterprise Resource Planning (ERP) platforms. In Aberdeen's May 2011 study, *Streamlining Indirect Tax Management: Best Practices in Minimizing Audit Exposure*, the key objectives among stakeholders are to:

- overcome the interoperability challenges among tax and financial applications
- to capitalize on existing enterprise data useful for tax reporting purposes, to encourage the tax and IT departments to work collaboratively to meet compliance requirements
- to leverage automation (where possible) to reduce manually-induced errors

- to minimize business disruptions during the implementation-to-launch process

Figure 1 depicts the top pressures prompting tax managers to improve their current indirect tax management practices.

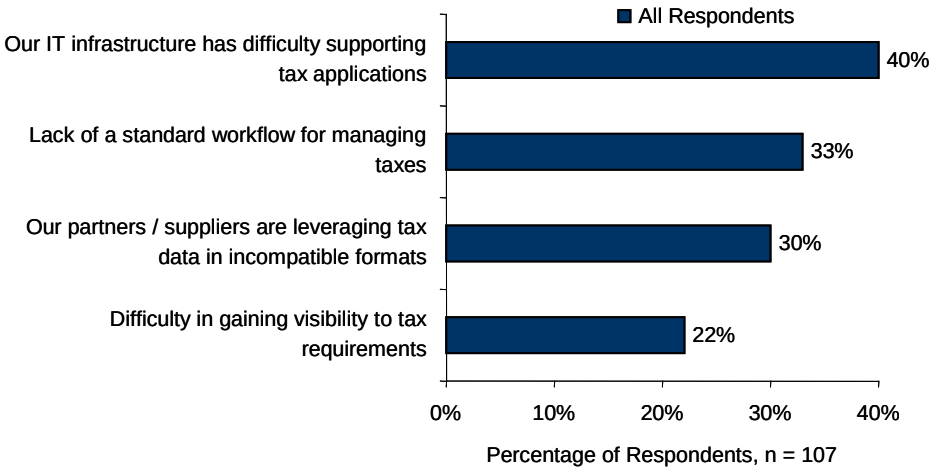
Figure 1: Pressures that Drive Better Tax Management



Source: Aberdeen Group, May 2011

Figure 2 reveals the top challenges faced by IT administrators when addressing the needs of the tax managers.

Figure 2: Challenges for Implementing Indirect Tax Management Solutions



Source: Aberdeen Group, May 2011

Strategies that Align Deployment and Compliance Objectives

When approached by tax and finance managers on solution implementation, the IT staff should remember that the cost of non-compliance impacts everyone. This impact stretches across to future budgeting needs as well. The common set of initiatives amongst the tax, finance, and IT staff is therefore to:

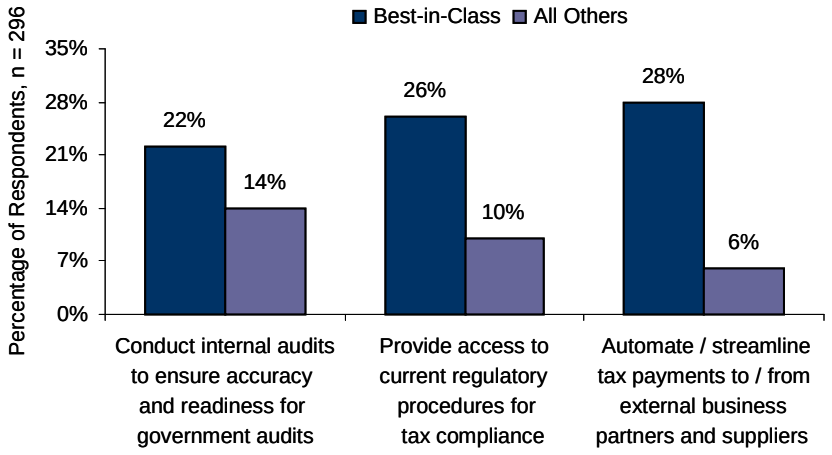
- Enable cross-functional collaboration between IT and tax staffs to ensure alignment between project and compliance initiatives
- Implement technology platforms to streamline tax data and information access, in order to accelerate preparation, filing, and remittance activities
- Accelerate the tax and ERP integration process to minimize business (compliance) disruptions
- Maximize staff productivity by implementing tax management technologies that allow the tax managers to focus on compliance, and the IT administrators to focus on project completion
- Deploy best-of-breed financial solutions that interoperate well with ERP platforms to improve access to enterprise-wide data relating to tax compliance

To support these initiatives, these stakeholders must share a common set of strategies, as depicted in Figure 3.

"Automation of tax collection and reporting allowed us to move from collecting / remitting in 23 states to doing so in all states without increasing staff."

~ Director, Tax Management, The Orvis Company, Inc.

Figure 3: Top Strategic Actions



Source: Aberdeen Group, May 2011

From the ERP standpoint, Aberdeen's October 2011 report, *ERP's Impact on Finance Executives: Visibility Leads to Stability* report, found that Best-in-Class organizations are developing a set of the specific capabilities. The first group combines ERP and tax management applications in order to streamline information access and accelerate financial activities. By implementing a

Best-in-Class Criteria

The following were used to determine the Best-in-Class in Aberdeen's May 2011 study, *Streamlining Indirect Tax Management: Best Practices in Minimizing Audit Exposure*, with top-performers achieving impressive results in:

√ Reduction in tax fines and penalties

√ Reduction in operational cost

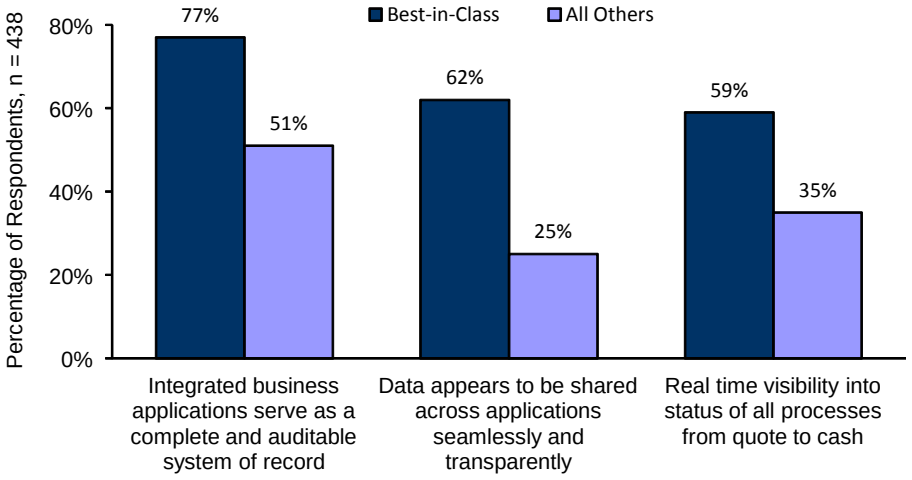
Best-in-Class: top 20% of aggregate performance scorers

Industry Average: middle 50% of aggregate performance scorers

Laggard; bottom 30% of aggregate performance scorers

complete system of record, and sharing information among applications transparently, Best-in-Class organizations are providing their financial employees with full visibility into their business from quote to cash (Figure 4).

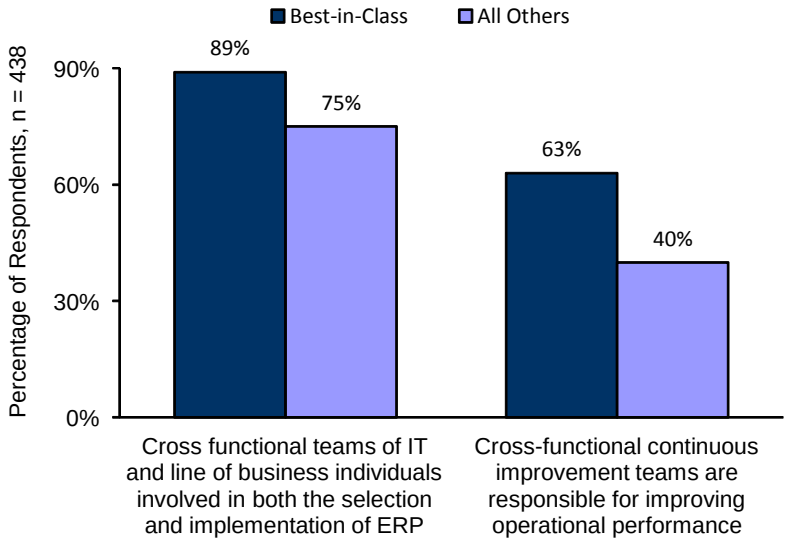
Figure 4: Integrated Systems



Source: Aberdeen Group, October 2011

Before that can happen, however, everyone needs to be on the same page. Line of business professionals, such as those in the finance department, need to collaborate with IT in order to set their needs for ERP along with its extensions such as tax management (Figure 5). These teams should continue to be involved in order to ensure that the systems that are implemented align with processes. For the finance department, this is in hopes that the solution provided can facilitate the tax and ERP implementation process leading to accelerated preparation, filing, and remittance activities.

Figure 5: Identifying What is Needed



Source: Aberdeen Group, October 2011

Best-in-Class Criteria

The following were used to determine the Best-in-Class in Aberdeen's 2011 *ERP's Impact on Finance Executives: Visibility Leads to Stability* report, with top-performers achieving impressive results in:

- √ Days sales outstanding
- √ Days to close a month
- √ Operating margin growth over the last two years
- √ Percentage of complete and on-time shipments

Table 1: Top Performers Earn Best-in-Class Status

Definition of Maturity Class	Mean Class Performance
Best-in-Class: Top 20% of aggregate performance scorers	▪ **33%** reduction in cost of government audit penalties / fines for the past two years ▪ **19%** reduction in time dedicated to addressing tax errors for the past two years ▪ **21%** reduction in administrative costs as a result of ERP ▪ **3.28** days to close financial statements at the end of the month
Industry Average: Middle 50% of aggregate performance scorers	▪ **3%** increase in cost of government audit penalties / fines for the past two years ▪ **12%** increase in time dedicated to addressing tax errors for the past two years ▪ **13%** reduction in administrative costs as a result of ERP ▪ **5.79** days to close financial statements at the end of the month
Laggard: Bottom 30% of aggregate performance scorers	▪ **3%** increase in cost of government audit penalties / fines for the past two years ▪ **35%** increase in time dedicated to addressing tax errors for the past two years ▪ **9%** reduction in administrative costs as a result of ERP ▪ **8.54** days to close financial statements at the end of the month

Source: Aberdeen Group, May / October 2011

Key Takeaways

Facilitating the integration of ERP and tax management solutions provide benefits throughout the business. For those in IT, it simplifies their workload and provides superior support in a more direct manner. For the finance department, it ensures alignment between the solutions being provided and the real problems they face in their day-to-day jobs. The evidence lies in the 19% reduction in time dedicated to addressing tax errors that Best-in-Class organizations have been experiencing in the past two years, and the 21% reduction in administrative costs that these companies are achieving as a result of streamlined tax integration with ERP. Both CIOs and Chief Financial Officers (CFOs) should take note of the following recommendations:

- **From a cost-saving perspective,** merging ERP and tax management means less custom software development, less custom application integration, re-use of available ERP financial data, and streamlined compliance to reduce audit exposure, and potential fines and penalties.

- **From a compliance-improvement perspective,** merging ERP and tax management leads to better audit transparency and results. Visibility is gained through technology into transaction history for both billing and procurement taxes. Further, this leads to easier support on sales expansion initiatives by having a scalable platform that maintains a tax schedule for various states and jurisdictions.

With these strategic initiatives in hand, CIOs can significantly contribute to the tax compliance of the organization, all while reducing operational costs and audit risk exposure.

For more information on this or other research topics, please visit www.aberdeen.com

Related Research	
Streamlining Indirect Tax Management: Best Practices in Minimizing Audit Exposure; May 2011 *Managing Value-Added Tax (VAT) in a Global Environment*; January 2011	*ERP's Impact on Finance Executives: Visibility Leads to Stability*; October 2011 *The Finance Employee's Approach to Managing Risk and Change*; August 2011

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