



Stat accounts count

Against the background of the focus on risk assessment by HM Revenue & Customs, the Senior Accounting Officer (SAO) regime, and the imminent imposition of mandatory iXBRL-based corporation tax online filing, Tax Automation director Bryony Clinton reflects on the importance of statutory accounts for each legal entity within a group, the related need for accurate accounting and tax data, and the pressure this can place on in-house tax departments.

Statutory accounts and their importance for in-house tax departments

Evolution

Takeover after takeover. Reorganisation after reorganisation. That's the way many large groups have evolved.

Some have developed as homogeneous groups. Others have grown into diverse conglomerates. Typically, efficiencies have been sought by merging similar activities and common support services and by cutting out dead wood.

Such evolution has left many in-house corporate tax departments worried that they may be relying on data they can't trust, from a variety of disparate sources they can't control.

Shortcomings of existing systems and data

Striving for growth and profitability, Boards provide overall direction while senior management focuses on operations and divisions. Financial controllers use software tools to produce management accounting reports that reflect operational hierarchies.

Enterprise resource planning (ERP) systems assist in managing internal and external resources and smooth the flow of information between business functions within the group. Financial consolidation software systems draw the different data flows together to present an aggregate view of the group as a whole.

ERP and consolidation systems centralise data, eliminating internal barriers caused by multiple software systems, standardising forecasting and reporting, while allowing business processes to work across functional boundaries. They are not a universal panacea – often expensive to install, difficult to customise and too rigid for many groups. In the way such systems are applied, blurring of company boundaries can cause loss of accountability. Installations are often tailored by external consultants to suit the perceived management needs of finance and reporting teams – tax is rarely considered.

By contrast, tax departments must have close regard to each corporate legal entity within the group; it is for each component body – not each operational division – that they

must prepare corporation tax returns and computations. It's rarely an easy task to achieve this in apparent conflict with the management accounting processes.

Customisation of ERP and consolidation software is complicated and expensive – as is the resulting maintenance burden. Some large groups are now shying away from this and moving back to 'vanilla' installations. However, this can be bad news for tax. Typically, vanilla systems don't deal with UK tax issues very well at all – especially as most ERP and consolidation systems emanate from the US.

Increasing use of shared service centres can make these problems even worse. Core back-office and other business functions are taken away from staff in operational divisions and delivered back to those units by specialist teams. Benefits may include reduced cost, enhanced quality and timeliness. Conversely, a downside can be that the support functions (and their accountability) become one step further removed from the real business.

The importance of statutory accounts

Too often, tax staff must assume responsibility for ensuring timely completion of statutory accounts for each subsidiary company, since it is they who must submit these to Companies House and HMRC by the respective statutory deadlines. These accounts are generally seen as having no other purpose, making it difficult to inspire finance colleagues to do the necessary leg work. Indeed, tax departments are commonly blamed because their tax planning activities are often seen as creating the need for additional entities.

It can be an uphill struggle for finance to prepare statutory accounts where corporate identities are obfuscated within divisions – or even worse, their activities are spread across multiple divisions – and where services are shared. But for tax and company law purposes, the accounts of each legal entity do matter.

Failure to produce the individual statutory accounts with reasonable accuracy could prejudice the rights of creditors, expose the directors to unlimited liability and attract HMRC penalties. Failure to maintain adequate systems and processes for getting the accounts and CT computations right could also count against the Senior Accounting Officer under the SAO regime – invoking penalties and reputational damage on both the group and the individual.

The impending move to iXBRL, to improve HMRC's data analysis capabilities, adds a new dimension. From 1 April 2011 all company accounts and corporation tax computations submitted to HMRC for accounting periods ending on or after 1 April 2010 must comply with this new data format. Third party CT software will be readily available to produce iXBRL-compliant computations, but software choices for producing iXBRL statutory accounts may be less plentiful. For some, iXBRL will simply confirm what they've always misguidedly thought – that statutory accounts are required primarily for tax purposes.

Many groups perceive that proprietary accounts preparation software is not sufficiently flexible to meet their needs. There may be few alternatives as the market in iXBRL-enabled accounts preparation is still immature. Groups that retain greater flexibility by using Microsoft Word or Excel may face difficulties in converting their output to iXBRL format. Many large groups face a fundamental reappraisal of how they prepare the statutory accounts of all their component entities.

Although HMRC has promised a ‘soft landing’ on penalties for those who fail to meet the stringent iXBRL requirement at the outset, this will only apply to companies that have made a reasonable attempt to comply, so solutions should be sought sooner rather than later.

Assuring the quality of tax data

Here at Tax Automation, we think that tax departments need to ‘own’ the data they need to focus on legal entities – or otherwise establish controls that verify to their satisfaction the accuracy of such data. Otherwise, how can they possibly vouch for the tax returns and computations they prepare, and the statutory accounts that are prepared primarily for them to submit to the authorities?

Tax personnel need to know that the data they hold is correctly attributed to each entity and accompanied by all the tax-sensitive information required. Many in-house tax teams will have addressed this already as part of their ongoing risk assessment discussions with HMRC, and in the course of producing documentation needed to prove compliance with the SAO legislation.

Group by group, the approach that works best will vary. In some cases the priority may be to establish a hub of detailed company information - including the structures of divisions, business units and legal entities along with tax balances and related administrative details. This might help reconcile and control issues that arise where legal entities and operating divisions diverge, supporting not only compliance but also tax and treasury planning.

In other instances the approach might be to create a tiered structure of reporting packs that pull relevant data from the group’s ERP and consolidation systems, facilitate improved analysis by operational or business unit, and then apply the appropriate tax rules – always reconciling back to the individual statutory entities in a robust and auditable way.

Change as an opportunity

Within the past few years, the introduction of HMRC’s risk assessment process and the imposition of onerous new obligations on SAOs have created ideal opportunities for groups to consider their tax processes and procedures.

Between now and April 2011, change will focus more on procedures for preparing statutory accounts, as groups grapple with the issues involved in ensuring that these are iXBRL-compliant. This generates a business case for reviewing data-gathering systems and ensuring that they comply with demanding new requirements in a well-controlled and cost-efficient manner.

What better time could there be for tax departments to make sure the entity-based statutory accounts, on which so much depends, are fit for tax purposes?

Contact us

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