

Tax Reporting in Taxing Times

This article examines the pressures faced by in-house tax departments in a period of accelerating change, and considers how their technology requirements can best be met in the current financial climate.

Unsettled economic times

The credit crunch is having some interesting side-effects. Predictably, as in any economic downturn, IT budgets are among the first to come under pressure. Companies are becoming increasingly reluctant to embark on new projects. Senior management, when evaluating potential costs and benefits, are inclined to set the bar even higher than usual, reflecting their mounting aversion to risk.

In spite of this understandable need for caution, groups are under pressure to streamline their financial reporting processes and comply with ever more demanding accounting standards. A recent report published by KPMG (*Finance of the Future – looking forward to 2020: May 2008*) envisages that quoted companies will move to reporting their results – with appropriate tax provisions – first quarterly and then monthly, and envisages that by 2020 there might even be pressure to report results on a daily basis! These ever more rapidly changing patterns of reporting will create new challenges for finance and tax functions and the ERP (enterprise resource planning) systems on which they substantially rely, together with business reporting and consolidation systems such as Hyperion.

Changes in reporting patterns

Within corporate tax departments current workloads are driven by existing half-yearly and annual reporting cycles, monthly, quarterly and annual tax compliance processes, and ongoing tax planning requirements. In acquisitive groups merger and acquisition activity and other special projects place additional demands on senior tax staff. Any move to increase the frequency of financial reporting could have a dire impact on the already time-consuming processes of gathering tax information from individual companies (which are viewed

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as separate entities by tax authorities) and consolidating these into group tax charges (which need to be reflected in the consolidated financial reports).

When it comes to ERP systems the needs of tax departments are not well served. Tax is often overlooked when new ERP installations are designed and implemented, perhaps on grounds that tax is too specialised or complex, or simply because the needs of the tax function are neither recognised nor understood by some external systems integrators advising the business. Furthermore, ERP systems do not typically contain sufficient functionality to produce the tax numbers; instead, they may provide the necessary inputs from the business and store the computed tax answers but this fails to address the alchemy between these. This remains the exclusive province of tax personnel.

Conflicting IT demands

Understandably, when IT projects are being prioritised, senior management are on the lookout to champion those that relate to tasks which not only are mission critical but also differentiate the company within its marketplace. Likewise, ERP suppliers come to the party with their own priorities, none of which usually involves tax. Most tax activities (planning, compliance, reporting, M&A) are indeed mission critical and have to be done well to avoid putting the business at risk. However, they fall short of being key differentiating factors: inventing better ways to produce tax computations will not gain customers or increase market share. In planning IT for the business, therefore, tax remains a neglected niche.

Increasing administrative burdens

In spite of the Government's stated aim of reducing administrative burdens on

business, changes in UK tax compliance requirements impose additional strains on already over-stretched internal tax resources. We don't have to look very far for examples. While consultations on the UK taxation of foreign profits have slowed down and are likely to be extended over a much longer period than originally expected, there are fears that the proposed new regime for 'controlled companies' may eventually reappear and could impose substantial extra compliance work on companies with overseas subsidiaries. Similarly, the current European Commission proposal that VAT returns be submitted monthly instead of quarterly threatens to impose enormous additional burdens on large companies and groups – particularly those with complex partial exemption calculations.

Other factors, too, can cause uncertainties. Large companies and their advisers and auditors do not always agree on how to interpret international accounting standards, and changes in view becoming apparent shortly before sign-off may impose intolerable consequential pressures on tax staff forced to re-jig tax calculations at the last minute. Such problems can be expected to arise frequently as standards evolve – for example, if (as seems likely) IAS 12 is tweaked to incorporate FIN 48 and other aspects of FAS 109 to facilitate adoption of IFRS in the US.

Even against this background finance and tax functions are not immune from cutbacks. While an economic crisis is never the best time to persuade management to invest for the future, there may be problems ahead for companies that fail to recognise the growing pressures of heavier tax reporting requirements and the strains which these will place on their scarce tax skills and related systems and procedures.

Spreadsheets v databases

In their tax reporting processes many corporate tax departments rely heavily on spreadsheets. Much has been written elsewhere about the flexibility gained by using spreadsheets for gathering tax data from individual companies and compiling group tax figures, and about the difficulties of controlling the quality of multiple spreadsheets and providing appropriate audit trails. Some tax departments discover to their cost that there are practical limits to the extent to which such spreadsheets can be relied upon; shortcomings in maintenance can lead to unexpected crises and embarrassing accounting inaccuracies.

For tax personnel who may lack advanced IT skills, spreadsheets can be relatively easy to create and maintain, and they provide the user with wide-ranging functionality and flexibility in manipulating data. Tax specialists generally welcome the power that this gives them but it can be dangerous. Spreadsheets used by one individual may be indecipherable and virtually useless to anyone else, rendering the organisation vulnerable if the originator is redeployed or decides to move on. Spreadsheets used by a team may be created, used and maintained inconsistently by different users, leading to unexpected and irreconcilable errors.

Alternative workflow systems using a database approach can provide a safer tax reporting environment – with loss of flexibility more than compensated for by improved quality control. Corporate tax departments that use such systems to bring together the group tax figures and to manage related aspects, such as tracking the tax histories of heritable properties and other fixed assets, may find themselves in a stronger position to cope with the implementation of new accounting standards and the growing frequency of financial reporting.

Database-driven systems can offer specific advantages over their spreadsheet equivalents. For example, they can provide secure, multi-user access across networks, structured user level security, effective validation of data input and trouble-free carry forward of figures from one year to the next. Overall, they promise a more secure working environment and this is crucial now in minimising perceived tax compliance risk.

Bespoke database systems are not the only alternative to spreadsheets. There are 'off-the-shelf' systems that stand somewhere between the two and need to be configured to meet particular requirements. Some such systems originate in the US and may therefore need to be adapted to suit UK tax circumstances.



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Change is never popular. The task of migrating the work of an in-house corporate tax department from a myriad of spreadsheets to an off-the-shelf or tailored workflow solution can be a daunting exercise, and one which might be postponed or avoided too easily on grounds that the up-front costs are prohibitive. However, the costs of not exploring and implementing such options may prove to be much higher in the longer term.

Tax process review

The first stage towards improving tax workflow is likely to be a tax process review. Given the limitations of the enterprise-wide perspective taken by ERP suppliers, there are strong arguments for adopting a 'best of breed' approach and getting such a review carried out by specialists with in-depth knowledge and understanding of the in-house tax world. As tax professionals themselves, they will have the expertise to produce ideas and develop solutions that address the needs of those responsible for the tax processes.

The review will seek to identify and clarify the current tax compliance and reporting processes used, identify key risk areas that currently exist, and outline suggested improvements to the processes and technologies used within the tax department to mitigate those risks. Such a review can be crucial in putting the work of the department on a sounder footing, ensuring that it is better able to cope with future tax reporting demands.

Implementing improvements

Experience suggests that a 'big bang' approach is unlikely to be appropriate for any tax transformation project. Hard-pressed tax staff are much more likely to welcome incremental changes, concentrating on quick wins at the outset and leading on

to realise other benefits in stages until the ultimate goal is reached. Furthermore, such an approach may allow relatively small improvements to be applied, tested and optimised successively on an iterative basis.

Such a project might well start by improving the systems for tracking compliance progress, then gathering data to monitor tax positions and creating a tax knowledgebase using a 'tax dashboard' approach. After that it might move on to integrating more tightly the link between tax processes and ERP systems by bridging data between Oracle, SAP, etc and tax accounting and tax compliance tools – all still accessible through the tax dashboard. Finally the project might address more complex areas of tax, such as transfer pricing adjustments.

Other factors may enter into the equation. Uncertainties in UK corporate tax are persuading the boards of many large companies to look closely at their international structures and question whether they wish to remain UK-resident for tax purposes. Assessing the impact of existing and proposed tax legislation in a variety of jurisdictions requires accurate tax data flows from all component parts of the group; improved tax reporting processes should provide these.

The future of tax reporting

Looking ahead, the developing capabilities of XBRL (eXtensible Business Reporting Language) are likely to have a part to play in future tax reporting methodology. The power of XBRL will make it an attractive feature of accounting systems, and XBRL tagging at the transaction level has the potential to improve dramatically the quality and range of management information flows and audit trails. Under the latest SEC proposals, about 500 of the largest companies would be required to file XBRL-based financial statements, starting early in 2009. Under current UK legislation all companies will have to file XBRL-based accounts and tax computations with their Form CT600 tax returns from April 2011.

Large companies with complex group tax affairs should beware the risks involved in cutting back on tax technology expenditure when so many changes are afoot. This may be the right time, instead, to carry out appropriate reviews and introduce tailored incremental IT solutions, putting such companies in a stronger position to cope with future tax reporting obligations.

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