

Using Sarbanes Oxley to Initiate a Strategic Tax Technology Roadmap

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A Longview Whitepaper

SARBANES OXLEY – STRATEGIC TAX TECHNOLOGY ROADMAP

Inhale..... exhale..... deep..... slow..... step back..... think ahead. Imagine an end-to-end tax solution and process that is SOX compliant and enables your CFO, your auditors, or your Audit Committee to drill down on the income tax footnote and see the math behind the tax disclosures shortly after closing. A day when tax closes simultaneously with corporate accounting, with the accuracy required to file tax returns, all in accordance with well thought out and well executed tax plans. Imagine inverting the tax workload from 80% data manipulation and compliance to 80% planning and tax risk management. You can imagine the downstream effect on the tax defense process. Seven years later you can still see the rationale, the math, and the audit trail behind your global income tax numbers. In this new world with an end to end tax solution you are no longer putting out fires. You are in control. You have the luxury to be strategic, delivering value to your company and shareholders like never before.

Sounds like “pie-in-the-sky”?

The technology exists today to make this dream a reality. O.K., maybe an 80-20 version of this dream which would be very appealing to all of us (including our auditors). So why isn't Corporate America taking advantage of this tax technology? Because today's tax departments are under siege. They have been forced by the corporate governance craze to shift their focus from pure “tax” tasks (planning, implementing, complying and defending) to financial reporting of income taxes, tax risk management, Sarbanes-Oxley, internal controls, and remediation of significant deficiencies and material weaknesses. Understandably tax executives and their departments, being, overwhelmed by the SOX workload and the increased visibility of Corporate Boards, CEOs, CFOs and independent auditors, are head's down on these issues. They can't breath let alone think strategically as to how to improve the corporate tax workflow. However, for the strategically minded corporate tax executive and CFO, change is opportunity. In this new SOX world, these corporate leaders see the need and benefits to stepping back, assessing the current landscape, envisioning a greatly improved one and developing a roadmap to “Tax Nirvana”. How is this accomplished? Put your strategic hat on and follow these three steps:

1. Define your desired future state (Tax Nirvana)
2. Define your current state
3. Plot your plan for going from current state to future state

Defining Your Desired Future State: Tax Nirvana

I have spent a lot of time thinking about the concept of Tax Nirvana, how to achieve it and discussing it with customers. Based on these discussions, I believe Tax Nirvana can be defined as the end-to-end automation of that which is automatable in the continuum of the corporate tax workflow, a state where when accounting closes, tax closes with the accuracy required to file all jurisdiction's tax returns. In this place, the reported tax disclosures are timely, accurate and auditable. It is a state where through technology, processes are improved to automate the:

1. Collection of the data (book and tax) necessary to calculate accurate federal, state and international tax provisions
2. Calculation of the tax provision (global ETR and deferred taxes)
3. Reporting of all required disclosures via the income tax footnote
4. Administration of the tax return compliance process
5. Ability to engage in tax planning via a suitable sand-box of the company's global tax position and finally
6. Supporting the tax defense process and related information needs.

Defining Your Current State

In discussion with corporate tax executives they can readily define their current state as follows:

1. Inadequate legal entity book accounting
2. Charts of accounts that are not friendly to the needs of the corporate tax function
3. Excessive and broad use of Excel for data collection, calculation and tracking of permanent and temporary differences, provisioning, etc.
4. Significant return to provision true-ups
5. Significant deficiencies (and in some cases material weaknesses) in internal controls surrounding their accounting for income tax reporting and process.

All agree that the first order of business is a system that consolidates by legal entity. They refer to "legal entity purity" or simply getting good pretax book income numbers by legal entity. (Some struggle with simply identifying all of their legal entities, their related entity-classification and country of origin.) Roughly 80% of tax executives feel that their departments do too much of corporate accounting's job in producing book pretax income by legal entity. On top of their current tax and SOX remediation workload, the majority still struggle with reaching legal entity purity, see this as automatable and the first step on the road to Tax Nirvana.

In addition to the legal entity purity problem, many companies are desperately trying to figure out how to deal with Excel Hades. In a May 24, 2004 Computer World article researchers at the University of Hawaii found a 91% error rate in an audit of 54 spreadsheets. And, The Journal of Property Management stated on July 1, 2002 that when an Excel spreadsheet has more than 200 line items, the probability of error approaches 100%. Given the current internal control environment, the use of Excel between more than a few users with more than a few lines is no longer acceptable. That presents a real problem for 90% of corporate America, tax departments included.

These problems are certainly understandable (although no longer acceptable) given the complexities of the multinational corporate business environment and past technologies. With each new acquisition comes new and different ERP's, general ledgers, and charts of accounts. Add to that the hundreds if not thousands of legal entities and taxing jurisdictions across the globe. On top of that, consider that the typical global tax department collects Excel tax packages from potentially hundreds of division controllers who are not experts in tax or FAS 109 income tax accounting. When you put it all together, you can see that the current state presents no small challenge for process and technology improvement. However, that same complexity presents untold opportunities.

Getting from Current State to Tax Nirvana

Couple today's technology that is driving new and improved processes with a multi-year roadmap and you can, in fact, automate that which is automatable along the continuum of the corporate tax workflow. If the required logic and math can be built in Excel, it can be built in today's more suitable technology: platforms that use the same architecture, database and user interface as that used by corporate accounting. Technology that self-validates data collected to the book numbers, translates where necessary and consolidates automatically and in real-time. Technology that can automatically collect, process and report consolidated book income on a tax adjusted basis by legal entity, by jurisdiction.... immediately when corporate accounting closes. Wow! But how is this accomplished?

First, it requires an open mind to simply envision such a state of Tax Nirvana. Don't balk at such an idea as strictly pie-in-the-sky, but rather embrace it even for the 80-20 potential opportunity. When I present this vision to our Fortune 1000 multinational customers and prospects, they get it immediately. They also question how they'll get from current state to future state with the limited and stretched resources at their disposal.

Second, draft a high-level executive summary of a Strategic Tax Technology Roadmap. This is typically a multi-year plan for going from your current state of tax processes and technologies to a state where your book data

automatically populates tax provisioning functionality (pretax book income by legal entity, those permanent and temporary differences that are simply changes in year-end balances, etc.) and which automatically populates your income tax footnote and your income tax compliance system. The executive summary should highlight the costs and benefits to the company and why it should be approved and prioritized.

Third, present this vision and high-level roadmap to your Controller, VP of Finance and CFO. They will immediately understand the financial reporting and internal control benefits of using the same database, the same software and the same user interface for both GAAP and tax reporting. Seeing that accounting and tax can now move in lockstep, they will provide the executive sponsorship and budget required to successfully institute change in global organizational behaviors.

Fourth, create a project team consisting of a cross-section of financial reporting, corporate accounting, tax, legal, treasury, IT and divisional controllers to draft the details of the roadmap in accordance with your company's typical project management process. To get this right, accounting, tax and operations must work together.

Finally, recognize that the road to Tax Nirvana will take a few years. But it can, will, and is happening. Human behavior simply needs to catch up with current technology. It's all about People, Process and Technology. It's about leadership and the tax executive and CFO seizing the Sarbanes Oxley challenge to generate strategic benefits for the company. It's about taking action now, however small, and in deliberate steps as the future unfolds. It may take a while to get there, but as you approach the land of Tax Nirvana the significant benefits realized by your company, your employees and you make it worth the journey.

About Longview Solutions

Longview Solutions provides corporate performance management (CPM) and tax reporting software that leading companies such as Trustmark, Time Warner, Home Depot, Eaton, Welch's, and Integrys use to drive performance with speed, visibility and financial integrity. Since 1994, many of the world's most respected companies have been using Longview to create a single repository of financial truth from which all, or any one of the following key financial processes can be performed: Financial Planning, Budgeting, Forecasting, Modeling, Disclosure Management/XBRL Reporting, Statutory Consolidation, Management Reporting, Profitability Analytics, Tax Provisioning, Uncertain Tax Positions and Tax Data Warehouse. Longview is headquartered in Toronto, Canada with additional offices in Philadelphia, Chicago (USA) and London (UK). For more information visit www.longview.com.

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