Digital transformation and tax: 
Time for a new operating model?

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Introduction 3
Pressure outside-in 4
Embracing technology 5
Altering the dimensions of work 6
Changing established processes 7
Rethinking resourcing 8
Assessing organizational maturity 9
Mapping the way forward 10
Let the modernizing begin 11
Introduction

Many tax administrations are digitizing their interaction with enterprises, reshaping digital filing and reporting requirements and they are digitizing their audit techniques. A recent example is the Making Tax Digital plan in the United Kingdom. Also, the Organisation for Economic Co-operation Development (OECD) issued its Base Erosion and Profit Shifting (BEPS) guidance in November 2015, calling for greater international cooperation and information sharing. By the end of 2017, the Inclusive Framework on BEPS counted 110 jurisdictions among its members—and many of its provisions had become enshrined in many domestic tax laws.

As a result, businesses confront the possibility of greater scrutiny, more tax audits and digitization requirements. But these are not the only pressures. Internally, tax functions are increasingly challenged by the board to have more efficient operations so they can focus more on delivering insights to senior decision makers. At the same time, the digital wave disrupting whole industries is now making its way to the tax function.

All this has renewed discussion among CFOs and tax directors about how to run the tax function in an increasingly complex environment. Reimagining the operating model has implications for the way tax works, the resources it needs, and how it must evolve in the face of unrelenting change. But to unpack these implications, it is first necessary to understand the role that technology, talent, and processes play in capturing a potential opportunity for change.
Pressure outside-in

Figure 1. Tax Administrations are digitizing across the globe (not exhaustive)

Tax Administrations of 48 countries united in the Forum on Tax Administration working group of the OECD developed a roadmap in 2016 to grow into Digital Tax Authorities. The essence is that they transform their own working processes to be more digital, and more importantly, that they will focus on data as a valuable source rather than as a residual product of tax compliance processes. That also allows them to work in the present: a real-time data driven tax environment.

Since 2016, the participating countries engaged in strategic pilots, sharing information on lessons learned and best practices on a quarterly basis. The challenge for enterprises is to cater all specific local country needs as there is no agreement on how to implement digitization initiatives of the 48 countries. This requires enterprises to comply with new or enhanced requirements and enterprises are confronted with smarter Tax Administrations.

As a result, the tax function needs to be more upstream in the enterprise in order to manage the initial entry of data. Controls needs to be preventive and automated rather than detective, and before Tax Administrations get a chance to perform analysis. In short, tax functions need to prepare to manage their global tax positions proactively, and with at least equal means as Tax Administrations will have available.
Embracing technology

As other parts of the organization adopt new technologies, more tax functions find themselves under a mandate to do the same. In the vanguard are robotic process automation (RPA) and cognitive computing (figure 2).

Another megatrend that is changing how the tax function operates is big data. The advent of powerful analytics tools has turned massive data volumes into potential sources of intelligence. As a result, firms are treating data less as an operational by-product and more as a fungible asset that can further the interests of the business. To the tax function, this means data can not only help improve the compliance process but may also yield projections and insights that influence the direction of the organization.

What makes these trends disruptive rather than evolutionary? One big reason is how accessible the technologies are to users across the enterprise, including tax. For a long time, business analytics was the province of a group of specialists in the IT department who built reports upon request using licensed on-premises software. Now business users can carry out their own analyses using platforms they subscribe to online. As for RPA, the technology is designed to work with existing systems. Much of its value lies in automating small tasks (that add up to a lot of extra time), which it does by recording keystrokes and other human-to-machine interactions.

Therefore, implementing RPA can in many cases be a do-it-yourself project.

This kind of value is a welcome boost to tax functions under constant pressure to do more with less. Tight turnaround times often accompany both regulatory compliance and ad hoc management requests. At the same time, business and regulatory changes can leave tax challenged to restructure their accounting and financial reporting. Under the circumstances, technologies that offer a cost-effective, noninvasive way to eliminate error-prone manual processes are increasingly likely to get management’s attention.
As technology shifts, the workforce is shifting along with it. The old construct—often with top-down hierarchies, large staffs, and siloed processes all on the same campus—is giving way to something new. Labor is becoming more diverse, more autonomous, and more remote. Innovation and leadership are growing more democratic. Collaboration and agility increasingly define top-performing organizations (figure 3).

For tax leaders, the convergence of technology and talent creates potential opportunities to rethink the organization along three dimensions: what people will be doing (work), who can do the work (workforce), and where the work is done (workplace).

- **Work.** In the future, people can work alongside automation, cognitive, and AI technologies—with technology picking up the bulk of manual and repetitive work.

- **Workforce.** For their workforce, the tax organization of the future can assemble a portfolio of human and machine labor. The labor can be full-time, contingent, or even crowdsourced (contributed from a community).

- **Workplace.** Technology can enable collaboration, integration, and line of sight among geographically dispersed teams. In turn, tax leaders can identify the places, tools, structure, and practices for people to come together to create value.

As work becomes more automated, and the workforce more diverse, physical proximity will become less important than the ability to bring in the right people for the right job at the right time.
Changing established processes

Figure 4. A transformative solution may mean reimagining established processes

So how do these changes break down at the process level? One way is to look at how tax ordinarily carries out work versus what it can look like post-digitization (figure 4).

Today, tax teams are often impeded by sequential processes. Consider that analytics may not happen until after year-end when the books are closed and the tax returns are done. Staffing levels are similarly rigid. However, digitization enables both processes and labor to flex as needed, allowing tax to respond to business needs as they occur.

Another hallmark of the current state is a lack of standardization. Tax functions often deal with different business units, regulatory jurisdictions, systems, and processes. This creates redundancy, forces manual workarounds, and gives rise to errors around compliance and reporting. However, emerging technologies, as previously mentioned, can bring automation and control with a minimum of disruption.

Then there are workpapers—those forms that require tax professionals to gather data and manipulate it so that it can fit, potentially wasting time and duplicating effort with each iteration. Digital enhancement can allow preparers and reviewers to work directly with the raw data, efficiently searching out the information they need and reconciling it only once.
Rethinking resourcing

Given these and other opportunities for improvement, some companies are taking a fresh look at their resourcing models. Historically, the approach has often been to carry out the tax function’s responsibilities with little to no help from technology, automation, or third parties. However, concerns about the historical model’s sustainability are prompting organizations to consider alternatives (figure 5).

One of those alternatives is insourcing. With this model, firms carry out production work via a mix of staff, company-operated shared service centers, tax technologies, and process automation. The insource model can be highly effective when paired with smart decisions about headcount reductions or functional reorganizations, process improvements, and tax technology enhancements. Another requirement is talent to help with the transition from manual to automated tasks.

The outsource model has a similar structure but sources the production work from a third-party service provider. Typically, this kind of service provider has the economies of scale to achieve significant process automation as well as appropriate levels of specialized staffing. A recent trend is for companies to request a full outsource of global compliance functions, with strategic teaming to achieve organizational objectives in specific planning areas.

As for shared services and tax technologies, these can remain in-house or not. A common approach among companies with an outsource model is to combine internal and external resources—for example, they might keep the company-specific shared services and technologies in-house while outsourcing the rest.

Most recently, an operate model has emerged in which the organization turns over all, or nearly all, of its tax function for a third party to operate. This may involve the deployment of an integrated technology platform as well as the talent transfer of corporate personnel to the third-party service provider.

Organizations that take this approach may have been challenged to modernize their technology or secure new talent. Either way, they seek to reduce many of the variable costs associated with tax—from licensing and implementing software to hiring, training, and retaining qualified talent.

The takeaway? Companies have a number of alternatives for resourcing their tax processes. Whether it is insource, outsource, operate, or another model to be discovered, the most suitable one is the one that aligns with the culture and demands of the organization.

Lessons in restructuring

Restrurugings are subject to certain types of oversight. Moving to a shared services center, for instance, can break the international tax process unless a plan is in place to:

- Address intellectual property structures
- Keep up with local legislative changes
- Interact with local tax administrations

Meanwhile, outsourcing tends to direct attention on the processes under transition at the expense of the ones left behind. To avoid this pitfall, tax leaders should consider how they intend to:

- Reassign retained talent
- Rework the business processes that stay in-house
- Adapt in-house technology to work with the outsourcer’s systems

Be it shared services, outsourcing, or a hybrid of the two, preparedness—as always—is key to a smooth transition.

Figure 5. Traditional tax functions can progress to an insource, outsource, or operate model
Assessing organizational maturity

Figure 6. Tax operations can land on any path along the technology maturity curve

If the business is to mature over time, then the tax function should be prepared to mature along with it. This requires a dedicated approach to understanding where tax is today and where it could go. It also requires an understanding of how tax can mature over time (figure 5).

In the static phase, tax operations has limited technology, little or no automation, and a limited number of controls for tax risk management.

The reactive phase brings some standardization and basic automation to help improve efficiency and control.

Organizations become proactive once they adopt a portfolio of tax applications that help people manage documents, check on project status, set up calculations and reporting, and collaborate with others responsible for a given process.

Progressive is when tax operations employ fully integrated enterprise and tax solutions for data collection and warehousing, advanced workflows, and real-time analysis and reporting.

The point of a maturity assessment is not to judge the tax function’s performance. Instead, it is intended to establish a baseline of current capabilities. That may turn out to be right where the organization needs it to be, wherever it lands along the continuum. But if the organization needs more, it now has a baseline for figuring out where it needs to go.
Mapping the way forward

Determination to modernize tax operations may be necessary—but insufficient. CFOs and tax leaders also must have a practical plan of action. These seven considerations can help the organization bring the changes they need to fruition:

1. Defining a tax function vision.
   Focus on a shared vision of key characteristics that define what the tax function will look like in three to five years.

2. Understanding perspectives and expectations.
   Gain insight from tax stakeholders and customers. Identify challenges that transformation initiatives can address.

3. Assessing effectiveness.
   Confirm the key competencies of the tax function and determine what opportunities may exist to improve performance or create more value for the business.

4. Prioritizing opportunities.
   Consider the future tax function, identify a subset of responsibilities to focus on based on the potential value to the organization, and then set priorities to help decide how resources should be invested to make the greatest impact.

5. Developing initiatives and mobilizing.
   Dig into root causes and identify potential approaches to address high-priority competency areas. Develop an action plan with key milestones and owners.

6. Confirming the function’s commitment.
   Identify areas of confidence and concern relative to executing against the tax function’s initiatives, and commit to specific actions.

7. Securing buy-in and funding.
   Up-front and periodic stakeholder interactions can help provide the knowledge needed to integrate the transformation with the business.

These steps seem intuitive—and they are meant to be. But each step builds on the ones before it. Skipping one can undercut the effectiveness of a transformation effort. At the same time, each step that is completed can make the next one easier to carry out.
Let the modernizing begin

BEPS, digitization of tax administrations globally, the drive for continuous improvement: Each of these is a powerful force. Together, they form a crucible that CFOs and tax directors can use to forge a new model for their tax operations.

There is no single formula for bringing this about. A number of models can be effective, depending on the needs of the organization. But they should be the product of careful consideration around the role of technology, the dimensions of work, and the process for achieving tax goals. Add strategic sourcing and a clear view of the future, and tax leaders have the foundational elements they need to turn a time of disruption into a historic opportunity.
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