Tax Function of the Future

Spotlight on:
Tax Organization Design: Options to manage Global Tax in a post-tax reform world

pwc

The *Tax Function of the Future* series spotlights topics relevant to Tax with a focus on *what Tax needs to do now to operate successfully* in an increasingly complex tax and business environment.

The Tax Function of the Future series predicted challenges that Tax functions may face now or in the future and offers correlative solutions. Our prior papers presented insights on topics ranging from new legislative and regulatory challenges to evolving tax operating sourcing models with emphasis on implications for technology, data, people, and process.

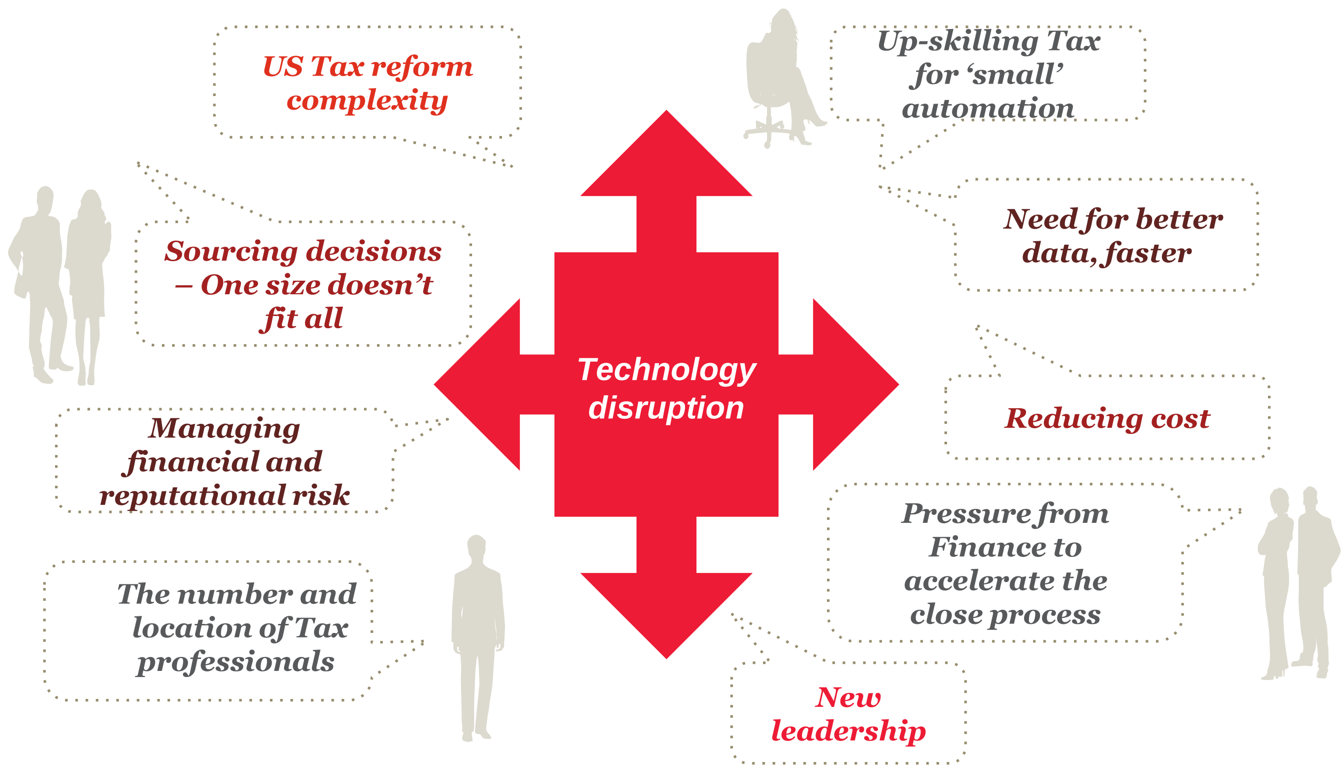
For more information on our predictions and prior Tax Function of the Future publications, please visit www.pwc.com/us/futureoftax.

In an environment that is still reeling from the most sweeping US tax reform in thirty years, we now expand our discussion on tax sourcing models to explore, more broadly, the organizational structure of the Tax function. What are the factors driving Tax leadership to consider a change? How do various design elements impact an assessment of what the optimal model is? We will describe the benefits and risks associated with the four typical tax operating models and explain how Tax functions can get started on a path towards a structure that is best suited for their operational success.

Catalysts for change: Why rethink organization design now?

These are complex times – Environmental and internal business challenges require that Tax be adaptable to change. The main catalysts for re-evaluation of the department's structure are summarized below:

<u>The Challenges Facing Tax</u>



US Tax Reform

The 2017 Tax Cuts and Jobs Act resulted in new calculations and considerations throughout the tax lifecycle. Tax must now contemplate:

- Are the right numbers of people working on the most relevant issues and associated computations? Are people strategically located in geographies to enable tax efficiency and operational execution?
- Do I have the right skills and capabilities to manage planning and controversy in a new regulatory environment, in addition to accounting for new modeling and computational elements that will be required?
- Does the lower tax rate free up funds to focus on enhancements to varying aspects of the Tax functions operational and organizational model?
- How could technology address new tax reform requirements? Should technology be built in-house, purchased outright or acquired through some blend of co-sourcing or outsourcing?

79%

of executives say US tax reform allows them to make strategic investments they would not have made in the past.

Source: PwC, How Tax Reform affects Business Strategy: 2018 Survey of the C-Suite, June 2018

Finance processes

Finance and other enterprise functions have made strides in streamlining processes and are investing heavily in technological upgrades. Can Tax keep up with internal demands?

- Faster finance close cycles require quicker access to information and closer connection with the business for real-time decision making
- Routine tax calculations and reconciliations need to be done faster and accurately for the income tax provision
- Finance organizations are achieving efficiencies by using shared service centers. Should Tax also participate in these new centralized service delivery models and are can they reap similar benefits?

Cost reduction

Often, Tax is perceived as a cost center, facing constant pressure to do more with less. How do cost containment or SG&A reduction efforts affect Tax?:

- Analysis of the number of Tax professionals needed to perform tax work in-house, as well as evaluation of those activities that are value-add versus time wasters and non strategic
- Special consideration to whether streamlining activities and the man-hours devoted to them may be achieved through some blend of co-sourcing or out-sourcing of some tax activities

Technology

Available and emerging technology is the constant catalyst driving change across business functions – And Tax is also impacted by this widespread disruption.

- Global finance transformation is moving enterprise systems to the Cloud and causing a fresh look at system design and reporting enablement
- Tax must consider innovative ways of collecting and processing financial data, moving away from the manipulation and reconciliation of data to more forward thinking analytics and information collection for real-time decision making
- The emerging trend towards 'small' automation empowers Tax professionals to be innovative without the need for big IT involvement. Do Tax professionals have the skills needed?

Tax function design elements: How to approach structuring Tax

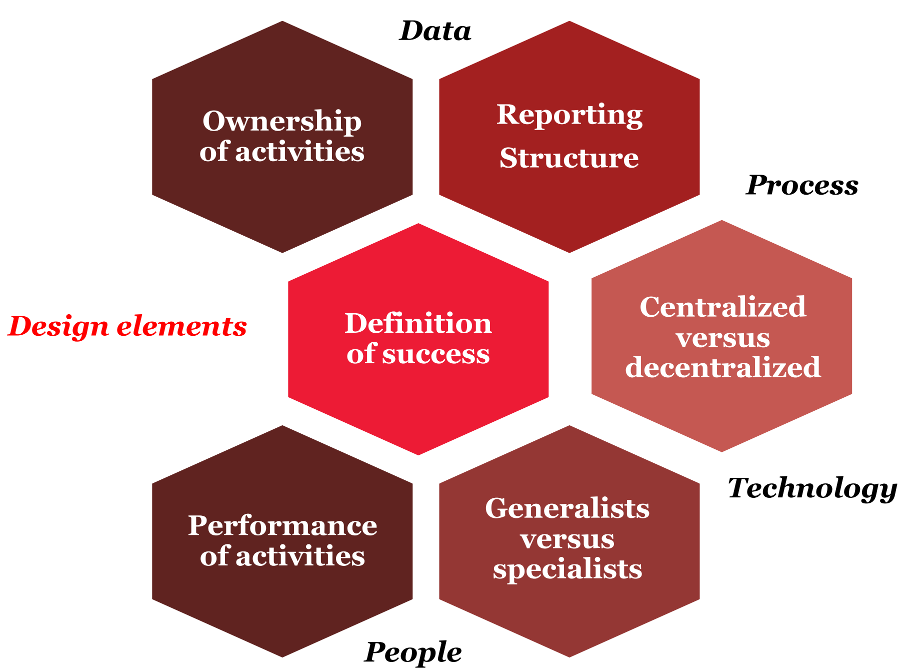
The question of how Tax departments should be structured is contemplated frequently. Tax functions come in many sizes and dimensions due to the variety of elements that shape design. Tax will need to determine how these elements apply within their broader organization to move forward on designing an effective operating structure. Let's examine the most critical tax function design elements.

The definition of success

The very first consideration is an understanding of what defines success for the Tax function specific to your organization. In our Spotlight publication, *Defining Success: What KPIs are driving the Tax function,* we define broad key success factors for Tax;

- Tax cost (Strategic tax planning)
- Tax risk (financial and reputational)
- Efficiency and effectiveness
- Sustainability of tax positions

Awareness of these and other success factors, along with focus on specific priorities and measures that are important for Tax, will enable the definition of remaining design elements comprising the organization's operating structure.



The reporting structure: Who does Tax report to?

For most large multinational organizations, Global Corporate Tax reports to the Chief Finance Officer (CFO); however, for smaller or decentralized regional or local tax operations, the Tax function may report to the Corporate Controller, Treasurer or other executive. Why does it matter who Tax reports to? This hinges on the broader organization's strategic priorities and the value that is attributed to the Tax function. During these complex times, it is important for Tax – even if only at the corporate headquarters level – to have access to the C-Suite, to share tax opportunities, risks and the impact that Tax has on the broader organization. Tax can no longer be a downstream consumer of data, focused primarily on reporting activities but must now more than ever be a strategic business partner, enabling access to critical data for business decision making that impacts the organization.

Direct exposure to the CFO or Finance leader with regular access to an organization's senior leadership will raise Tax's profile with the potential to influence change within Tax and throughout the broader enterprise.

Where is the Tax work performed – Central headquarters or decentralized business units?

Since good understanding of the broader business is essential for tax planning, compliance, reporting, and controversy support, Tax would benefit from the integration of Tax professionals into business operations, with alignment to the region or business unit they support. Corporate Tax is generally focused on consolidated compliance and reporting in addition to planning, transfer pricing, and controversy support on a global, consolidated group level. How then should Tax manage from the center while staying relevant to business operations and the impacts of planning on the overall organization?

Tip

Although embedded in the business, professionals operating in decentralized Tax departments should retain dotted line reporting to and close working relationships with Corporate Tax for alignment on priorities, objectives, and performance development.

What activities should Tax own and perform?

Often, the Tax department owns all direct and indirect taxes, including income, sales and use, value added, payroll and property taxes. Some Tax functions even take on responsibility for business licenses and statistical reporting. Should Tax necessarily own any and all types of tax?

We believe that some activities are best managed by the functions that are closest to the data and own the business processes most closely tied to tax generation. For instance, payroll and property taxes may be more efficiently handled by Human Resources or Operations due to the specific payroll and property related information required for tax compliance.

Tip

Tax should develop the business case to support ownership transfer of certain taxes to functions that are better prepared to gather and interpret relevant data (such as payroll and property). However, absence of formal ownership should not prevent Tax from offering technical tax support, as able. Tax should collaborate with all enterprise functions in the best interest of the overall business.

Once Tax has agreed with the business on the activities it should own, in line with strategic priorities for success, the function must determine whether it actually performs these activities in-house. Does the department have the capacity, expertise and technology infrastructure to efficiently and effectively deliver? Could some routine functions be performed by an enterprise shared service center? Some level of complexity may require co-sourcing or out-sourcing to a third party service provider. In our initial publication, we predicted the following; however today's sourcing options have expanded, ranging from in-house to complete outsourcing or managed services.

PwC prediction:

Most global tax preparatory compliance and reporting activities, including data collection and reconciliations, will be performed within the company's shared service center or will be co-sourced with a third party.

Tax often retains the highest-value activities in-house; however, in many cases, even those activities are out-sourced to manage risk. International tax planning, controversy support and transfer pricing are areas where the largest, most sophisticated Tax functions still rely on third-party expertise.

Who does in-house tax work – generalists or specialists?

An important element of Tax function design is the alignment of talent to the tasks that will be owned and performed internally. Is the Tax department small enough, based on enterprise size or decentralized structure, to deploy generalists who can satisfy all requirements throughout the tax lifecycle? Larger Tax departments tend to organize activities based on specialty functions. Typical specialty areas are US income tax reporting and compliance, international tax compliance, indirect tax reporting and compliance, strategic international tax planning, transfer pricing, and controversy.

Within these broad specialty categories, there are many variations. For instance, US state and local planning and compliance may be handled by a dedicated team of professionals. Similarly, income tax returns may be prepared by professionals working closely with the team calculating the income tax provision. What is important is that the right people are deployed with the proper skills needed for the task at hand. Are the skills and capabilities of the personnel aligned to strategic priorities?

The emergence of new technologies (such as machine learning, robotics, and blockchain) and the growing interest in 'small automation' add important dimensions to today's Tax function design. Tax professionals are now expected to leverage tools that perform small-scale automation smarter and faster. How does this trend affect the need for tax technologists? Tech-savvy Tax professionals will be in increasing demand, either as a specialists within a larger organization's tax technology group or embedded within the function, aligned to a particular specialty area, such as indirect or income tax compliance.

Over time, as technology skills continue to develop, the typical Tax professional will be comfortable performing tax technical functions, while navigating the tools and systems that make work easier. Technology also enables remote capabilities that allow flexibility for professionals to operate efficiently from various locations around the world.

Tax leadership should constantly monitor Tax professionals' satisfaction with deeper concentration in an area versus broad exposure to most tax activities. Training, cross-functional rotations and interaction with multiple business units may result in a more enriching job experience.

Common tax operating models

Having defined success, established strategic priorities and considered design elements, Tax should evaluate the operating models available to engage Finance and the business in achieving the function's success. We will describe four basic structural operating models with varying degrees of in-house and externally sourced services. Tax functions may deploy aspects of several of these models in defining their optimal operating structure:

In-house Tax function

Description:

Typically used by large global organizations for decades, this structure utilizes a corporate tax headquarters function, with decentralized regional or business unit tax departments as well as local controllership led execution in foreign jurisdictions. Substantially all tax activities are performed in-house.

Key benefits:

- Tax support is closest to the business with potential to build cross-functional relationships, gather information needed at its source, and assess business decisions for their impact on tax in real-time
- May provide broader development experiences across a variety of tax functions

Risks to manage:

- The decentralized Tax department is remote from Corporate Tax leadership; Tax needs to ensure alignment with Corporate priorities, performance development and succession planning
- Tax professionals may report to the regional or business unit Finance Controller or Treasurer without direct access to senior leadership
- Disparate, non-standard systems and processes may evolve over time

Shared services enabled function

Description:

This structure involves a centralized Corporate Tax function that leverages broader finance shared service centers or centers of excellence for routine, transactional, and highly repetitive tax activities, retaining other tax activities within the confines of the corporate tax umbrella.

Key benefits:

- Systems and processes are standardized since all tax activities are managed by the center
- Provides access to dedicated, trained resources with ability to scale rather than decentralized segments of full time equivalent/employees (FTE's)
- Opportunity to collaborate more closely with Finance and other functions utilizing enterprise shared service centers
- Potential for lower cost of delivery

Risks to manage:

- Attrition resulting from low job satisfaction within the shared center due to lack of role formalization and growth opportunity
- Limited skills and ability to handle more complex tax matters
- Lack of connection to the business and day-to-day issues that drive tax matters

Strategic co-sourced / outsourced environment

Description:

In this structure, the centralized Corporate Tax function co-sources or outsources select processes to a third party and retains management oversight, leveraging external knowledge, technology and resource investment.

Key benefits:

- Allows internal focus on strategic, high-value activities
- Provides access to expertise and technology not available in-house
- Offers flexibility to co-source or outsource for a defined period of time while building internal capabilities

Risks to manage:

- Decouples elements of the tax life cycle, potentially resulting in some inefficiency
- Third-party providers are further away from the business – lacking relationships and ability to quickly gather information

Fully outsourced managed services function

Description:

This structure does not include any in-house tax expertise; therefore, all tax activities are outsourced to a third party with the Corporate Controllership owning the externally sourced Tax function. In some cases, substantial segments of the business' Tax department are outsourced, including the management of those activities. This structure is referred to as "managed services".

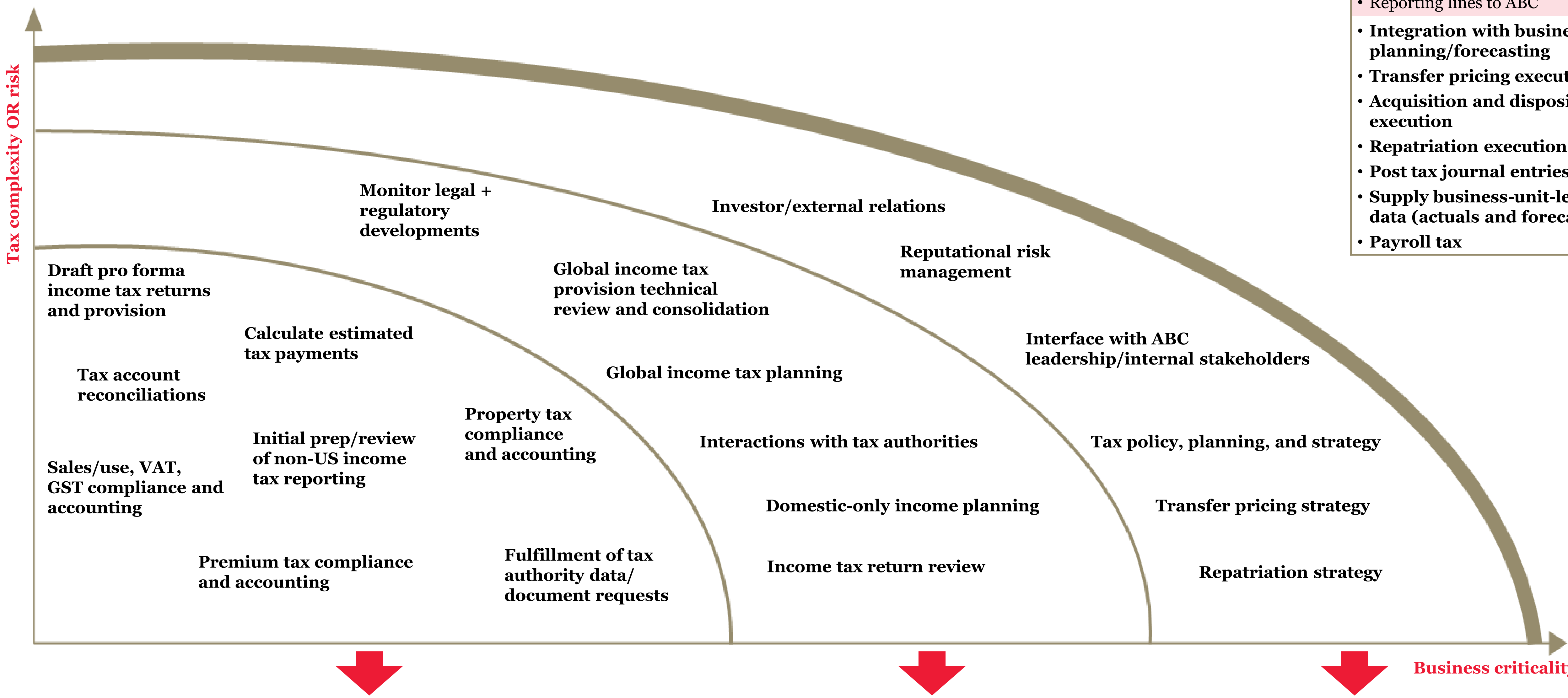
Key Benefits:

- The business acquires tax expertise and streamlined processes, managed by the appropriate levels of leadership
- The flow of the tax lifecycle is kept intact
- Resource development and technological investment are managed entirely by a third party
- Technology is integrated with the tax lifecycle
- Tax team with an 'in-house' feel

Risks to manage:

- Less direct linkage to the business
- Requires substantial advanced planning and coordination for transition and stand-up

Example of a Global Corporate Tax Structure (Centralized leadership, with shared service center, Center of Excellence (CoE) and business unit execution)



Business unit ownership

- Critical functions only
- Limited to Finance-integrated areas and areas of “natural fit”
- Reporting lines to ABC

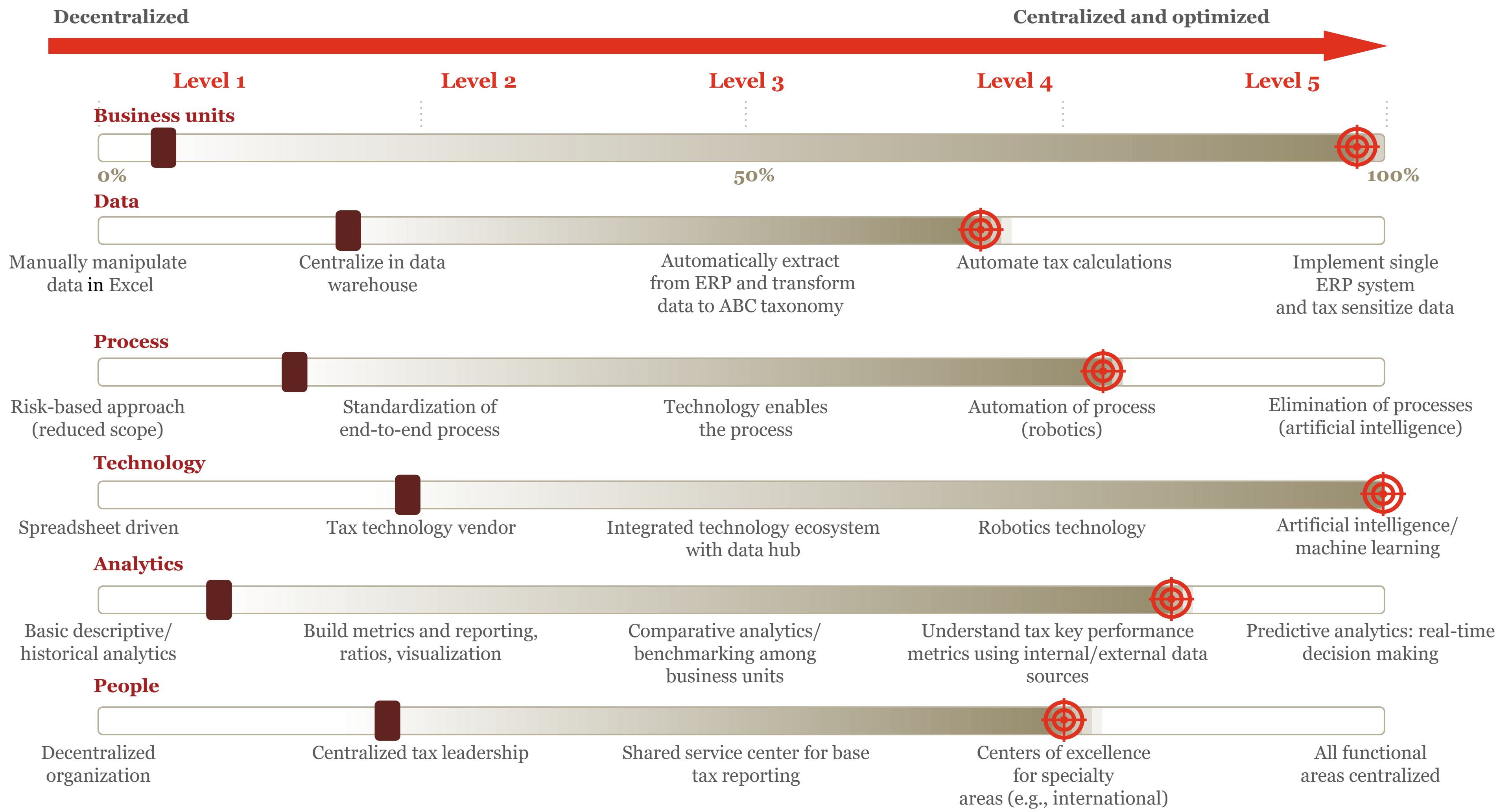
- **Integration with business planning/forecasting**
- **Transfer pricing execution**
- **Acquisition and disposition execution**
- **Repatriation execution**
- **Post tax journal entries**
- **Supply business-unit-level data (actuals and forecasts)**
- **Payroll tax**

Shared service center	Global centers of excellence	Centralized leadership
• Centralize repetitive tasks • Use established service provider platforms	• Scaled experience surrounding tax specialties (federal, international, transfer pricing, etc.) • Use service provider specialists	• Establish tax policies • Focus on high-value-added activities

The stakes are high as the Tax environment continues to change with technology disrupting the way we live and work. How should a Tax function begin on the path to a structure that best addresses their strategic priorities? Begin with an assessment – and be honest. Ask yourself what is going to define success for your organization and be realistic about which KPI's mean most. Decide collaboratively with others in your organization as to which activities the tax function should own in the first place. Strategically align processes and technology to the data and business activities that underpin them, and begin to define the skills and capabilities that will be required for your optimal operational model.

Does the current structure include the desired design elements? There will be trade-offs. Leveraging centralized models will require technology investment as an enabler, and creating the ability to have access to information for real-time decision making will be critical for Tax as a key business adviser to the broader organization. The graphic below illustrates the levers that can be moved to achieve your desired design for a corporate Tax function. You will need to take a close look at technology, data, processes, and impact to people as you assess the various desired design elements targeted for the organization's structure
and success.

Getting started with a Tax Organization Design Planning Matrix (example of decentralized to centralized Tax design planning)



Connect with us

To have a deeper conversation about how these issues and predictions may affect you and your business, please contact:

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