KPMG

cutting through complexity

TAX

Good, Better, Best

Russia

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Introduction

For the KPMG network, a top priority is helping member firm clients manage tax transformation and position their businesses for future success. Since 2006, we have conducted regular surveys of tax executives around the globe to uncover their most pressing issues. Our purpose is to gain insights on how these issues influence changes in structure, investments in people and processes, and overall objectives and priorities.

Now, in this updated survey conducted in late 2012, the environment in which tax directors operate has changed dramatically. Lingering economic uncertainty is increasing pressure on companies to cut costs and on tax authorities to boost revenue. Globalization continues to spur centralization of finance, tax and other functions. Companies are expected to improve their governance, accountability and transparency in all areas. Further, political attitudes toward taxation are shifting, with much more focus on civic responsibility and public demands that companies should pay their "fair share" of tax to the jurisdictions where they earn profits.

With this environment as a backdrop, we sought to identify trends and benchmarks on the following fundamental questions:

- How are tax departments changing their operations to address emerging economic, business and regulatory trends?
- How are they progressing on aspects of governance and performance such as strategy, risk management and measurement?
- How are they approaching process and technology investment and improvement, including the impact of cloud computing?
- How are they addressing the pressure to more effectively resource how they do their work?
- How are they responding to rising tax authority scrutiny and demands?

The survey now shows that tax departments have made good progress in several of these key areas. However, in a rapidly changing business and regulatory environment, the results also suggest that there is still work to do if tax departments are to meet the dual challenges of effectively managing risk while providing more effective, real-time support to business activity and influence on the bottom line.

Focus on Russia

Based on KPMG International's survey of tax executives, tax departments of Russia-based multinationals are:

- **Clarifying tax department accountabilities by adopting strategies that are consistent with the company's broader objectives**, but attracting less interest and guidance from boards and upper management in developing these strategies.
- **Improving tax department oversight by centralizing management and direction of the global tax responsibilities** within headquarters tax departments, generating gains in terms of greater global standardization of the tax department structures and processes.
- **Less likely to use outsourcing to support tax department activities** than their global counterparts, and potentially missing out on opportunities to free up tax department time to engage in other, more value-adding activities.
- **More focused on compliance, reporting and managing tax audits than other activities**, which limits their ability to collaborate with other departments and help with decision-making and other activities that add value across the organization.
- **Losing sight of the benefits of tax department connectivity as a consequence of centralization**, limiting the ability of their tax teams to collaborate with other departments and contribute value.

KPMG International's series of global benchmarking studies have charted the evolution of tax departments since 2006. Our 2009 study showed that leading tax departments – those that add the most value to their businesses – do so by putting high priority on three areas:

1. clarifying accountabilities
2. driving standardization and efficiency
3. promoting connectivity with their colleagues across the business in support of a proactive tax department.

In conducting the current survey on behalf of KPMG's member firms, we were keen to see how tax departments have progressed in these areas, especially given on-going economic uncertainty and continuing regulatory reform.

This report highlights insights from the survey on how tax departments based in Russia have advanced since our last survey in 2009. For analysis of the global survey results, read *Good Better Best*, and visit kpmg.com/goodbetterbest for more country reports, industry-related data, interactive tools and more.

Clarifying accountabilities – board involvement diminishes

Previous KPMG tax department benchmarking studies have shown that leading tax departments put priority on ensuring tax department's roles and responsibilities are clear and commonly understood within the context of a company-wide, board-approved tax governance framework. Compared to 2009, more multinational companies based in Russia have a tax strategy that is consistent with the company's overall business strategy – 92 percent of respondents in Russia reported having such a strategy currently, an increase from 73 percent in 2009.

However, the level of board involvement in tax strategy development and governance has diminished since 2009. The percentage of respondents in Russia who say their tax strategy has board-level approval dropped from 53 percent in 2009 to 42 percent in 2012. Further, only 58 percent say their board and/or corporate leadership are directly involved in providing guidance on the tax strategy – a slight increase from 2009 (60 percent).

92%
of Russia-based tax departments have a board-approved strategy that aligns with their overall business strategy

only 58%
of these strategies were developed with guidance from the board and/or corporate leadership

In the past three years, many respondents in Russia have sought to clarify accountabilities and improve the efficiency of their global tax management processes by establishing centralized tax departmments. The percentage of respondents who say their company has a headquarters tax function that directs, manages and coordinates the global tax function rose from 40 percent in 2009 to 78 percent currently. Additionally, 76 percent of respondents in Russia say they now have global standards related to tax policies and procedures (45 percent in 2009).

As we will see, tax departments in Russia have benefited from centralization in the efficiency and uniformity of their tax processes and controls. However, the rapid centralization of Russia-based tax departments may be hampering their ability to connect and collaborate with other business functions.

78%
of Russia-based respondents have a headquarters tax department, up from 40% in 2009

76%
have global standards for tax policies and procedures, up from 45% in 2009.

Driving efficiency – High standardization, low use of strategic sourcing options

Our previous research identified a focus on standardization to automate and strengthen tax processes and controls as a key characteristic of leading tax departments. Compared to their global counterparts, respondents in Russia report higher levels of standardization of their tax departments globally in most areas.

Controls and responsibilities and accountabilities of tax personnel were reportedly the most standardized area of tax departments in Russia, followed by tax policies and procedures. In terms of the annual tax compliance cycle (from forecasting through financial reporting, filing of returns and reconciliation), Russia-based respondents are also well ahead of their global peers, and standardization in these areas has increased since 2009.

Compared to their global counterparts, tax departments in Russia make less use of outsourcing, shared service centres or other finance resources to support tax department activities. Currently, 24 percent of respondents in Russia say they use outsourcing or co-sourcing to carry out or support tax department responsibilities, compared with 34 percent globally. Only 18 percent of respondents in Russia say they use a finance or accounting shared service centre to support tax department activities (30 percent globally), and 16 percent use other finance resources for this purpose (25 percent globally).

24%
of Russia-based respondents outsource tax department activities, compared to 34% globally

18%
use shared service centres for this purpose, compared to 30% globally

Interestingly, the 24 percent of Russia-based companies that do use outsourcing have increased their use of third-party providers for certain tax department activities since 2009. The types of tax functions that saw the biggest increases in outsourcing were tax controversy support (75 percent currently, up from 35 percent in 2009), tax planning and business support (58 percent, up from 0 percent in 2009), and statutory accounting/reporting preparation (42 percent, up from 12 percent in 2009).

However, the majority of companies based in Russia appear to be less inclined to outsource or co-source tax activities due to their stringent administrative standards and procedures and restrictive tendering processes, at least as far as domestic tax compliance in Russia is concerned. In our experience, foreign subsidiaries of Russian companies are more likely to make use of outsourcing to cover local tax responsibilities. By limiting their strategic use of outsourcing within Russia, businesses based in the country may be missing out on opportunities to free up in-house resources for other activities, to access best practices and investments that cannot be developed in-house, and to access specialized tax knowledge when business needs arise.

Promoting connectivity – compliance focus leaves less time for other activities

Connectivity with other parts of the business is crucial for tax departments to achieve their full potential as contributors to business strategy and drivers of value. Among Russia-based respondents, tax compliance and financial reporting activities take priority over other important tax department activities. While effective tax compliance is critical, the focus on these activities means that integration with business groups and early indication of routine transactions, for example, are given less priority, both in terms of how the tax function is measured and where tax function time is expected to be spent.

When asked where they expect their tax department would devote its time over the next 12 months, respondents in Russia gave the highest rankings to tax compliance and financial reporting. These activities are expected to occupy 17 percent and 31 percent of tax department time respectively. These respondents also expect to devote 10 percent of their time to managing tax authority audits.

On the other hand, integration with business groups and early indication of non-routine transactions ranked low in priority, expected to occupy only 7 percent of tax department time. Other value-adding activities—like optimizing the effective tax rate (10 percent) and cash tax planning (5 percent)—also are expected to take up less time.

Further, as noted above, tax departments in Russia have undergone rapid centralization since 2009. Despite the significant benefits of this restructuring for tax compliance and financial reporting activities, it appears that the balance has tipped perhaps too far away from connectivity. Compared to 2009, integration with business groups and early indication of non-routine transactions is significantly less important in driving tax department objectives in respondents in Russia. The centralization of other functions, such as mergers and acquisition teams and other finance functions, may be presenting further obstacles to connectivity.

Unfortunately, it seems likely that Russia-based tax departments in future may need to devote even more time to tax compliance activities, especially in their time spent dealing with tax authorities. Russian tax authorities have increased their scrutiny of outbound investments and foreign related-party transactions, collaborating and sharing information with foreign tax authorities and paying particular attention to tax-motivated business structures and issues involving business substance.

58%
of Russia-based tax departments' time is expected to be spent on compliance, reporting and managing audits

22%
is expected to be spent on optimizing the effective tax rate, cash tax planning, business integration and early indication of non-routine transactions

Respondents in Russia report that over the past 12 months, tax authorities have become more focused on auditing indirect, corporate and payroll-related taxes. Respondents report that the tax authorities are also more focused on reviewing tax processes and controls. Rising tax audit activity, combined with the compliance challenges that come with regional expansion, means that Russia-based tax departments may have to devote even more time and resources to compliance than they do now, leaving less time and resources to provide effective, real-time support to business activity and influence the bottom line.

However, for the majority of respondents in the country, there appears to be little interest in improving tax department processes to free up time for other pursuits. For example, 78 percent of respondents in Russia are satisfied with their current administrative budgets, 84 percent are satisfied with levels of investment in tax technology and process improvement, and only 10 percent expect the structure of their tax department to change in the near future.

Given the high compliance focus, forward-thinking tax directors in Russia should consider how they better balance the need to meet these obligations with other activities that contribute value. By making a business case for additional tax process and technology improvement, they not only stand to gain benefits in terms of greater efficiency and control over compliance and reporting processes. They can also free up resources to focus on higher value strategic and business support activities that are currently being neglected, allowing them to become more effective and proactive business partners that add value and influence the bottom line.

78%
are satisfied with their current tax administration budgets

Only 10%
expect their tax department to be restructured in the near future

Blueprint for change

As tax departments struggle to cope with mounting regulatory and cost pressures, leading organizations are seeing that a transformational approach can show the way forward. KPMG International's research has distilled the following steps as crucial elements in a tax department's blueprint for change.

1. Establish a **common purpose** by aligning strategic goals and objectives of the tax department with those of the wider company.
2. Define **one view of performance** to monitor effective tax management by clarifying requirements and how performance is measured and valued, through agreed-upon KPIs.
3. Ensure the tax department has **high-performing teams** with the right number of tax professionals and the right mix of training, skills and experience.
4. **Embed processes** to realize the tax management strategy in a way that is measurable and sustainable for the long-term.
5. Set systems and procedures to produce, exchange, and distribute **timely and accurate information** to the right people, at the right time, and in the right format.
6. Employ **enabling technologies** (e.g. enterprise resource planning systems, tax software) to automate labor-intensive processes that consume resources and increase risk.
7. **Influence stakeholders** by understanding their goals and constraints and communicating with them to help achieve the goals.
8. Set processes and priorities and align the tax department's structure to promote **connectivity and collaboration** between tax teams and other departments.

About the survey

- KPMG International's global survey of people in charge of tax policy and operations of businesses worldwide is one of the largest surveys of its kind.
- Iterations of the survey have been conducted regularly since 2006, charting the evolution of leading tax departments and identifying operational benchmarks for high-performing tax teams.
- For the 2012 survey, 1,150 heads of tax in 22 countries, including 50 respondents in Russia, took part in blind telephone surveys to share their opinions on how tax departments are adapting to current business challenges. About 700 of respondent companies are Fortune 500, Forbes 2000 or equivalent companies.
- To gain more clarity on the telephone survey results, additional in-depth interviews were conducted with several clients of KPMG member firms and tax professionals worldwide.

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