KPMG

cutting through complexity

TAX

Good, Better, Best

United States

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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 United States

Based on KPMG International's survey of tax executives, tax departments of multinational companies based in the United States are:

- **Drawing more attention from boards and corporate leaders,** primarily due to rising financial statement and reputational risk due to new tax and regulatory reporting requirements.
- **Reacting to intensifying pressure to reduce costs** by migrating tax activities to shared service centers and investing less in improving tax department processes and controls.
- **At risk of diminishing quality,** as shown by declining levels of global standardization reported by US-based respondents across the annual tax compliance cycle.
- **Putting high priority on tax compliance and reporting activities at the expense of other, value adding activities,** a situation that may worsen as US tax audit and controversy activity continues to rise.
- **In a position to make a strong case for increased investment in tax process and technology improvements** to help manage increasing compliance burdens while freeing up tax resources to engage in more strategic pursuits that contribute to the bottom line.

KPMG International's series of benchmarking studies of tax department structures and operations shows that leading tax departments – those that add the most value to their businesses – do so by putting high priority on three areas:

1. ensuring clarity of accountabilities
2. driving standardization and efficiency
3. promoting connectivity with their colleagues across the business through a proactive, outward-reaching tax department.

In the current survey conducted in late 2012 on behalf of KPMG's member firms, we were keen to see how tax departments have progressed in these areas, especially given ongoing economic uncertainty and continuing regulatory reform.

This report highlights insights from the survey on how US-based tax departments 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 – focus on tax risk and controls draws boards' attention

In the area of accountability, it is important to ensure that the tax department's strategic goals and objectives are aligned with those of the wider organization. For US-based multinationals, it has become common practice to have a tax strategy that is consistent with the company's overall business strategy – 93 percent of US-based respondents answered "yes" to this question, which is close to the result achieved in 2009 and in line with the current global result of 93 percent.

93%
of US-based tax departments have a strategy that aligns with their overall business strategy

Since 2009, the level of board involvement in tax strategy development and governance rose significantly. The percentage of US-based respondents who say their tax strategy has board-level approval climbed from 37percent in 2009 to 83 percent currently, and 80 percent of US-based respondents say their board and/or corporate leadership is directly involved in providing guidance on the tax strategy, up from 51 percent in 2009.

83%
of tax department strategies are board-approved

Several factors have prompted boards and corporate leaders of US-based global companies to take greater interest in how tax is managed in their organizations. Tax accounting lapses have been the one of the more common sources of material weaknesses and significant deficiencies reported in financial statements in the past few years. Tax risk has also become more visible due to US tax rules requiring companies to disclose their uncertain tax positions on their tax returns and balance sheets. As reputational risk related to tax for US-based firms has increased, executive and director-level involvement in tax risk oversight has risen accordingly.

This attention to financial statement and tax compliance risk is evident US-based tax departments' objectives and how they are measured. Accurate/ timely financial reporting and tax return compliance are considered much more important than other goals in driving tax departments' overall objectives in the coming year. Managing tax risk was named as the third most important. These are also the three most popular areas for which key performance indicators have been set.

Driving efficiency – cutting costs at the expense of quality?

Even though US-based tax departments face heightened tax risk, the current economic climate is putting them under increasing pressure to cut costs. As a result, US companies are investing less in improving in-house tax departments than they did in 2009 and than their global counterparts report currently. They appear to be shifting tax department activities to shared service centers and making less use of co-sourcing and outsourcing options in order to reduce expenses.

When asked what types of projects are in progress or under consideration within their tax departments, only 54 percent are improving their tax staff's training (74 percent in 2009; 61 percent globally), and only 46 percent are undertaking technology-related improvements (58 percent in 2009; 53 percent globally). Additionally, 57 percent of US-based respondents say they plan or are undertaking process-related improvements, compared to 63 percent in 2009 and 61 percent globally in 2012.

In contrast, US-based companies are investing slightly more in finance function improvements than their global counterparts. For example, 70 percent of US-based finance functions have undertaken global or regional process improvements in the past 12 months (68 percent globally and 60 percent have undertaken technology improvements (58 percent globally) and/or finance function strategic reviews (61 percent globally).

Further, US-based tax departments are less likely than their global peers to say they use outsourcing or co-sourcing to carry out or support tax department responsibilities. Results suggest that US companies are doing more work in-house in order to save costs. Only 24 percent of US companies use outsourcing (compared to 34 percent globally), while 29 percent use other finance resources for tax work (25 percent globally) and 27 percent use finance or accounting shared service centers.

As a result of the movement of tax work to shared service centers and other finance personnel, it is possible that a certain degree of quality is being sacrificed in favor of reducing costs. This can be seen from reported levels of standardization among US respondents. Having uniform processes in place generally increases the accuracy of tax data and related filings, simplifies the performance of routine tasks and facilitates the use of technology for monitoring and improving control. According to US respondents, since 2009, reported levels of global standardization have decreased across the annual compliance cycle, from forecasting through financial reporting, filing of returns and reconciliations of annual provisions and returns.

57%
of US-based tax departments are undertaking or considering process-related improvements, compared to **61%** globally

70%
of US-based finance functions have undertaken global or regional process-related improvements, compared to **68%** globally

Only 1/4
of US-based tax departments use outsourcing or co-sourcing to carry out tax activities, compared to **34%** globally

Only 1/2
use other finance resources and/or shared service centers for this purpose

Promoting connectivity – missed opportunities to contribute value?

As noted, among US respondents, tax compliance and financial reporting activities take priority over value-adding activities. Integration with business groups and early indications of routine transactions rank low in priority, both in terms of how the tax department is measured and where tax department time is expected to be spent. While effectively managing compliance is critical, other, more value-adding activities – like cash tax planning and optimizing the effective tax rate – are being pushed to the sidelines.

When asked where they expected their tax department to devote its time over the next 12 months, US respondents gave the highest rankings to tax compliance and financial reporting. These activities are expected to occupy 19 percent and 17 percent of tax department time respectively. However, only 7 percent of time would be spent on integration with business groups. Cash tax savings/tax deferral and optimizing the effective tax rate would occupy 10 percent and 11 percent respectively of tax department time.

Unfortunately, increasing tax audit and controversy activity at the federal and local levels means that US-based tax departments will need to devote even more time to tax compliance activities in the future, especially in their time spent dealing with tax authorities. US-based respondents report that in the past 12 months, tax authorities have become more focused on auditing corporate income and indirect taxes, as well as on reviewing tax and accounting processes and controls. According to respondents, managing tax authority audits is expected to occupy 11 percent of US tax departments' time in the next 12 months.

As a result, US tax teams will have even less time and resources to provide effective, real-time support to business activity and influence the bottom line. However, most US respondents show little interest in improving tax department processes in order to meet these challenges: 81 percent are satisfied with their current administrative budgets, and 80 percent are satisfied with levels of investment in tax technology and process improvement.

Further, 25 percent expect the structure of their tax department to change in the near future. Of these, reducing costs was first among the primary reasons for the change, named in 80 percent of cases, followed by increasing/improving control (52 percent). Better alignment with the business and/or finance function structure and needs were named as among the primary reason in only 20 percent of cases.

In summary, with tax risk rising, in both financial statement and reputational terms, the current focus on cutting costs may be short-sighted and could be putting quality at risk. In light of the challenges ahead, forward-thinking US companies should be considering their business case for additional investments in tax process and technology improvement. By doing so, they stand to gain greater visibility and control over tax compliance and reporting processes, higher levels of standardization, and improved accuracy. Just as importantly, they can free up tax resources to focus on higher value strategic and business support activities, allowing them to become more effective and proactive business partners that add value and influence the bottom line.

47%
of US-based tax departments' time is expected to be spent on compliance, reporting and managing audits

28%
is expected to be spent on cash tax planning, business integration and early indication of non-routine transactions

81%
are satisfied with their current tax administration budgets

25%
expect their tax department to be restructured in the near future, with "cutting costs" being the most commonly named reason

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 current survey, 1,150 heads of tax in 22 countries, including 100 respondents from the United States, 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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