Aberdeen Group
A Harte-Hanks Company

Streamlining Sales and Use Tax Management

Best Practices in Minimizing Audit Exposure

June 2011

William Jan

AberdeenGroup
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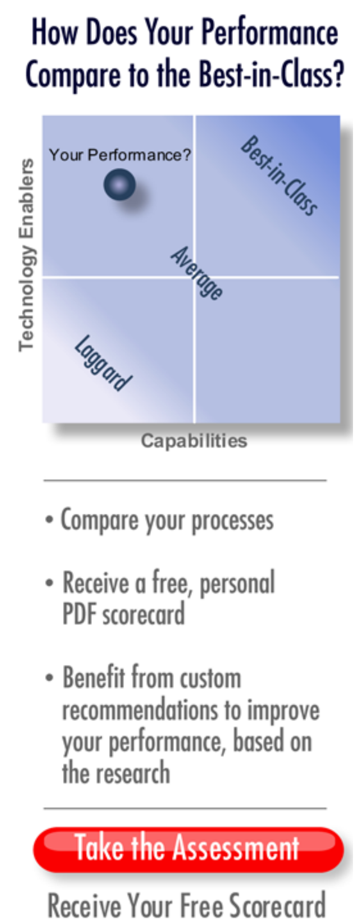
Executive Summary

Being exposed to government tax audits and having to deal with fines and penalties are issues that companies fear. The purpose of this report is to provide guidance on how best to streamline sales and use management. Nearly 300 companies were surveyed between April and May of 2011 to identify best practices and current capabilities in indirect tax management (taxes that are collected by vendors first from their customers, prior to remitting them to the state and local governments). The top-performing companies demonstrated that to achieve a high-level of success in managing transaction taxes (e.g., sales and use tax in the US, or value-added tax in various global regions) a strategic combination of process re-engineering and software automation must be implemented.

Research Benchmark

Aberdeen's Research Benchmarks provide an in-depth and comprehensive look into process, procedure, methodologies, and technologies with best practice identification and actionable recommendations



Best-in-Class Performance

Aberdeen used the following four key performance criteria to distinguish Best-in-Class companies: audit results, overpayment occurrences, cost reduction, and labor reduction. The performance levels of these top companies are as follows:

- 83% of all government audits, received in the past five years, yielded favorable results
- Only 7% of all reverse audits, performed in the past five years, revealed overpayments
- 33% year-over-year reduction in cost of fines and penalties
- 20% year-over-year reduction in staff time dedicated to addressing tax errors

Competitive Maturity Assessment

Survey results show that the firms enjoying Best-in-Class performance shared several common characteristics, including:

- 70% more likely than their competitors to possess an automated workflow from tax preparation to tax remittance
- 33% more likely than their competitors to have clear visibility into current tax rates and laws

Required Actions

In addition to the specific recommendations in Chapter Three of this report, to achieve Best-in-Class performance, companies must:

- Focus on maintaining sales and use tax domain expertise (whether in-house or via third-party solution / service providers)
- Be proactive, rather than reactive, in sales and use tax management
- Promote information transparency with state and local governments

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Benchmarking the Best-in-Class

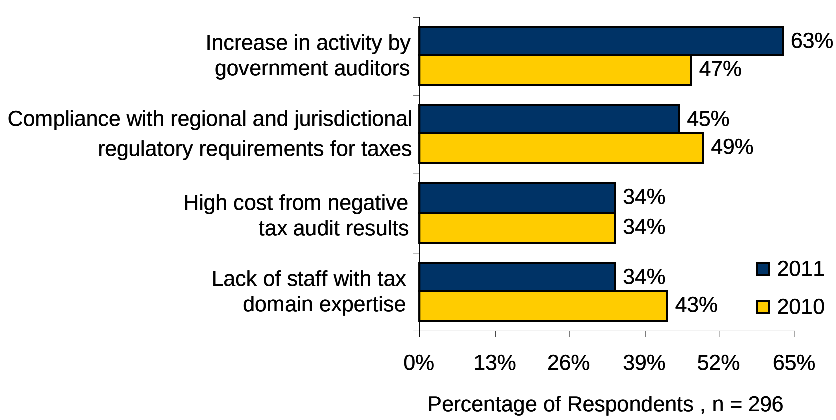
Business Context

State and local governments are experiencing revenue shortfalls, and audit activities are on the rise. The aim of this report is to establish a guideline for successful sales and use tax management. In Aberdeen's May 2010 study, *Effective Sales and Use Tax Management: Reducing Errors and Increasing Productivity*, over 100 companies were surveyed to reveal best practices in improving both the tax management process, and its underlying technologies. That said, this year Aberdeen focuses on how the sales and use tax landscape has changed in the past 12 months, how companies are affected by these changes in regulatory pressures, and their strategies to sustain their tax management practices. As a background, Aberdeen has reached out to a larger sample population this year (296 companies, to be exact, including tax managers and financial executives across multiple verticals), to support this new focus. The data was collected through two means: quantitative data analysis from electronic surveys and qualitative assessments through interviews. As mentioned in last year's report, state and local governments are increasing their audit initiatives against companies to compensate for their revenue shortfall. From the qualitative feedback that we've received from our tax community this year, not only has the momentum picked up among the auditors, but the expertise among these auditors is decreasing. This means that companies that are not transparent and proficient in their sales and use tax practices are opening themselves up to any potential fine or penalty that the government issues them - with no means of defense or protection. Experiencing government audits can be disruptive to any business, let alone the potential cost of an incorrectly-conducted audit. Figure 1 compares the pressures seen last year to those of this year with regards to drivers for effective sales and use tax management.

Fast Facts

- √ Best-in-Class companies are three times as likely as Laggards to standardize enterprise-wide procedures for tax preparation, filing, and remittance
- √ Best-in-Class companies are 105% more likely than All Others to have automated exemption / exception certificate management

Figure 1: Pressures that Drive Better Tax Management



Source: Aberdeen Group, May 2011

As the data reveals, there is a sharp increase in government audit activity in the past 12 months. And as expected, the cost of negative audit results remains high, while companies continue to struggle with compliance with various jurisdictional requirements. On the other hand, it is a pleasant surprise to see that companies have begun to take the concept of maintaining tax domain expertise seriously, whether these experts reside in-house or are third-party tax consultants. Some additional qualitative feedback that was received from our tax community includes the prioritization of sales and use tax versus other business taxes within their organizations. When looking at tax domain expertise, it would appear that many companies are seeking these experts mainly to manage corporate income tax, and that sales and use tax often earns less priority. What is troubling about this feedback, particularly with what we are seeing in our research, is that state and local governments obtain nearly 30% (usually more) of their revenue from sales and use tax. Thus they are becoming more motivated to increase their audit activities around this tax segment, in hopes to obtain more revenue. Companies should not be reactive to managing sales and use tax (seeking expertise only when being audited), but be more prepared (having an effective tax management and audit control solution and / or process in place) so they can counter these potentially high fines and penalties.

Finally, let us look at how governments are potentially targeting companies for audit. Last year, we found that many companies saw Mergers and Acquisitions (M&As), Initial Public Offerings (IPOs), and sharp growth in revenue as common trigger events for state and local governments to take action. This makes sense because:

- The aftermath of the credit crisis presented numerous opportunities for corporate consolidation
- The economic recovery prompted the execution of many IPOs (that were delayed due to the crisis)
- The recovery enabled earnings recovery across many industries

In short, these aspects all contribute to disruptions in business flow - disruption that can easily drive companies to misplace their focus on sales and use tax management. With the continued economic recovery, however, governments have changed their focus to maintain their revenue stream. Several companies have voiced to us that the government is now increasing their focus on large enterprise, with steady (but large) tax payments.

The Maturity Class Framework

Companies can only reduce their audit exposure and risk by being proactive in their tax due diligence process: making sure that numbers are right, and that the filings and the remittances are on schedule. These companies can do so by conducting internal audits to ensure accuracy and compliance. At times, internal / reverse audits do reveal overpayments to the government which also implies process inefficiency. That said, if a company were to be audited by the local government, it can expect the audit to trace back five years or more. To that end, Aberdeen used four key performance criteria to distinguish the Best-in-Class from Industry Average and Laggard organizations (Table 1).

Table 1: Top Performers Earn Best-in-Class Status

Definition of Maturity Class	Mean Class Performance
Best-in-Class: Top 20% of aggregate performance scorers	▪ **83%** of all audits in the past five years yielded positive results ▪ **7%** of all internal / reverse audits in the past five years revealed overpayments ▪ **33%** reduction in cost of government audit penalties / fines for the past two years ▪ **19%** reduction in time dedicated to addressing tax errors for the past two years
Industry Average: Middle 50% of aggregate performance scorers	▪ **50%** of all audits in the past five years yielded positive results ▪ **11%** of all internal / reverse audits in the past five years revealed overpayments ▪ **3%** increase in cost of government audit penalties / fines for the past two years ▪ **12%** increase in time dedicated to addressing tax errors for the past two years
Laggard: Bottom 30% of aggregate performance scorers	▪ **Lack of ability to track audit progress** ▪ **Lack of ability to track overpayments** ▪ **3%** increase in cost of government audit penalties / fines for the past two years ▪ **35%** increase in time dedicated to addressing tax errors for the past two years

Source: Aberdeen Group, May 2011

Between 2010 and 2011, the performance gaps between the Best-in-Class, the Industry Average, and the Laggards have widened. Companies that implemented best practices in sales and use tax management surged ahead of their competitors in the other categories. The notable difference is in the year-over-year decrease in the cost of penalties, fines, and corrective labor. Given that the size of penalties and fines is a function of tax amount difference and days overdue, the Best-in-Class demonstrate that the errors associated with their negative government audit results are of magnitudes smaller than those of the Industry Average or Laggards. Additionally, the Best-in-Class are the only organizations to achieve a year-over-year *decrease* in corrective labor, whereas all others (defined as the combination of Industry Average and Laggard companies combined) reveal an increase.

"Automation of tax collection and reporting allowed us to move from collecting / remitting in 23 states to doing so in all states without increasing staff."

~ Director, Tax Management, The Orvis Company, Inc.

The Best-in-Class PACE Model

Using effective solutions to achieve tax management goals requires a combination of strategic actions, organizational capabilities, and enabling technologies that are summarized in Table 2.

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Table 2: The Best-in-Class PACE Framework

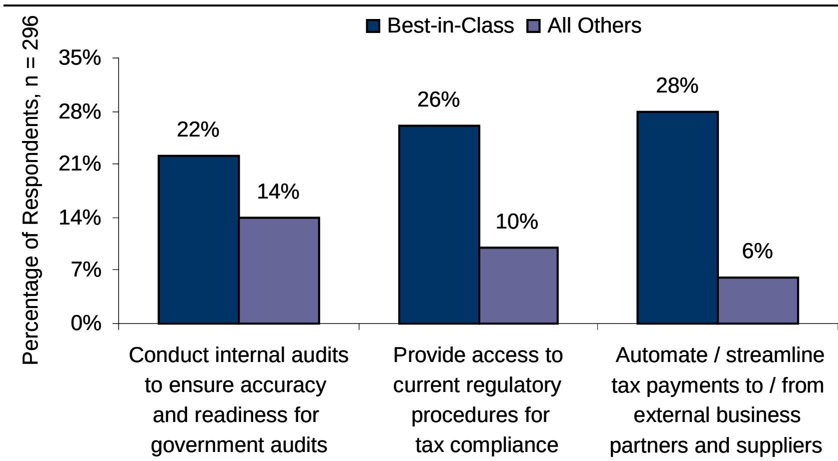
Pressures	Actions	Capabilities	Enablers
▪ High cost from negative tax audit results	▪ Provide access to correct tax rates for accurate calculations ▪ Integrate / streamline tax preparation, filing, and remittance processes	▪ Standardized enterprise-wide procedures for tax preparation, filing, and remittance ▪ Effective access to state, regional, and jurisdictional tax regulations ▪ Automated workflow from tax preparation to remittance	▪ Tax rates calculation solutions ▪ Sales and use tax preparation solutions ▪ Sales and use tax filing solutions ▪ Tax exemption certificate / exception management solutions ▪ Tax remittance tools ▪ Audit control solutions ▪ ERP systems with sales and use tax module ▪ Accounting software ▪ Professional services firms

Source: Aberdeen Group, May 2011

Best-in-Class Strategies

Improving sales and use tax management can contribute significantly to the reduction of audit exposure / risk, but many organizations lack the initiatives, capabilities, and technological enablers to mitigate such risks. Organizations realizing Best-in-Class performance have effective sales and use tax management capabilities as defined by a strong alignment of domain expertise to compliance measures, and effective technological enablers that allow stakeholder access to tax information and regulations for accurate transactions. The strategic actions of the Best-in-Class are identified in Figure 2.

Figure 2: Top Strategic Actions



Source: Aberdeen Group, May 2011

Despite that the Best-in-Class are about one-and-a-half times more likely than their competitors to provide effective tax rate visibility to their staff, and nearly five times more likely than their competitors to leverage tax automation capabilities with their partners and suppliers, the most notable difference lies in their proactive approach to managing taxes. By consistently conducting internal audits to ensure readiness for government audits, these top-performing companies are systematically mitigating their risks and reducing audit exposure.

Table 3 looks strictly at the statistics achieved by the Best-in-Class, Industry Average, and Laggard, with no correlations to the performance metrics used to define them in Table 1. Though it is impossible to establish a causal relationship between the number of internal audits conducted, and the number of government audits experienced, the statistics in Table 3 do seem to support the notion that being proactive has its rewards.

Table 3: Statistics on the Best-in-Class

Maturity Class	Mean Class Performance
Best-in-Class	▪ Conducted an average of **7.2** internal audits in the past five years (self or via third-party) to ensure accurate tax filings and readiness for potential government audits ▪ Experienced an average of **4.8** government audits in the past five years
Industry Average	▪ Conducted an average of **2.6** internal audits in the past five years (self or via third-party) to ensure accurate tax filings and readiness for potential government audits ▪ Experienced an average of **5.9** government audits in the past five years
Laggard	▪ Conducted an average of **0.0** internal audits in the past five years (self or via third-party) to ensure accurate tax filings and readiness for potential government audits ▪ Experienced an average of **6.3** government audits in the past five years

Source: Aberdeen Group, May 2011

Aberdeen Insights — Strategy

When comparing Table 3 to that of our 2010 *Sales and Use Tax Management*, one will notice that the number of government audits experienced has gone up across the board. This is in direct correlation with the trend that was discussed earlier regarding an increase in government revenue shortfall. But the important takeaway is the relative pattern between both years; in the past 12 months, companies that are proactive in their tax management practices are seeing a lower number of audits, as compared to their peers. This is in-line with one of the top strategic actions in Figure 2, where audit readiness initiatives should be implemented to reduce audit risk exposure and to maintain transparency with the auditors. The Best-in-Class are 57% more likely than their competitors to develop such strategies.

As companies are looking across the various tax disciplines associated with their businesses, whether they are around corporate income tax, employment tax, excise tax, or sales and use tax, being proactive in documenting transactions as if an audit were to occur will alleviate many problems down the line. It should really be more than just about people, processes, or tools to reduce risk and maintain compliance. It should be part of the company culture.

In the next chapter, we will see what the top performers are doing to achieve these gains.

Chapter Two: Benchmarking Requirements for Success

While last year's *Sales and Use Tax Management* uncovered staff productivity improvements through the effective automation of sales and use tax initiatives, this year's report focuses on how companies can best address the acceleration of government audit activities. The idea behind streamlining sales and use tax processes is more than cost savings and error reduction; it is about maintaining transparency to the state and local authorities (and possessing the means to defend against wrongful audits). To that end, Chapter One of this report covered how the Best-in-Class are able to reduce their corporate risk profile and cost through their proactive strategies and initiatives. Chapter Two takes a closer look at the mix of tax management solutions and domain expertise that enable a higher level of audit success and productivity.

Fast Facts

√ 63% of the Best-in-Class companies track the status of government audits while it is in session

√ 78% of the Best-in-Class companies have effective access to state, regional, and jurisdictional tax rates and regulations

Case Study — Addressing Government Audits

Changing economic environment and tightened credit markets have compelled businesses to search internally for ways to reduce operating costs and to streamline existing processes. However, many organizations are still relying on spreadsheets and manually entering critical sales and use tax data. The errors associated with these practices have contributed to negative audit results, subjecting the companies to heavy fines / penalties and high cost of corrective labor. Effective Sales and Use Tax (SUT) (also known as indirect tax or transaction tax) management can enable organizations to reduce tax overpayments, increase corporate productivity, comply with regulatory requirements and reduce the probability of negative audit results.

Karen Smith, Texas-based (Dallas) State and Local Tax (SALT) Manager, shares her experience from a previous role, where poor SUT management practices and culture were negatively impacting both tangible and intangible assets, in terms of net operating income and goodwill, respectively.

"I previously worked at a privately-owned company which underwent an acquisition and faced a severe reduction in staff. This resulted in several major compliance issues. For instance, sales and use tax liability accounts were not reconciled; consequently the company was unable to identify overpayment / underpayment incidents. In addition, most systems still relied on manual entry, as the company did not have any automated SUT management systems in place," states Smith.

continued

Case Study — Addressing Government Audits

Reluctance to adopt technology and automate processes is a common occurrence for many businesses as they view investment in such endeavors as expenditure, rather than as an investment. This mindset is being further augmented by liquidity issues experienced by companies in the new economic environment. According to our latest sales and use tax management survey, 39% of the respondents cited budget limitations for proper dedication of labor and solutions as a key challenge to undertaking SUT management initiatives.

Smith also stated that because many state and local tax audits were not done in a timely manner at the organization, the company lost credibility with the tax authorities, and were at risk of receiving Jeopardy Assessments [immediate Internal Revenue Service (IRS) seizure of assets, without prior notice, due to unreported income / customer tax collections].

“Executives tend to think of the tax department as a "step child." The department does not receive acknowledgement until the company receives a substantial tax assessment. Income tax tends to take a front seat in comparison to transaction tax. However, in the new economic environment, transaction tax is impacting a company’s bottom-line much more than income tax is,” explains Smith. According to Aberdeen research, finance executives at leading companies were twice as likely as those at Laggard companies to ensure the alignment of SUT management objectives with corporate strategy and risk profile.

”Upon getting hired, I decided to lead a tax reconciliation project. Consequently, the business was able to recoup $305K in overpayments of use tax for New Jersey. We also deployed an automated sales and use tax system which greatly improved the accuracy and efficiency of return filing,” states Smith. “We also hired a consultant to assist with auditing needs. It was therefore a strategic combination of technology and workforce that enabled the organization to transition to an efficient tax management system. However, most of these initiatives were born out of the necessity to resolve pending tax audit issues. Therefore, management addressed these issues on a reactive basis rather than on a proactive basis,” states Smith.

Smith believes that even though effective SALT management has a long way to go for many companies, current economic conditions have created a sense of urgency for them to take a hard look at their sales and use tax management processes, and to look for additional methods of reducing audit exposure, especially as states and cities face severe budget constraints.

In conclusion, companies that do business in a dynamic regulatory environment need to implement a mix of actions and capabilities to effectively improve transaction tax management.

Competitive Assessment

Aberdeen Group analyzed the aggregated metrics of surveyed companies to determine whether their performance ranked as Best-in-Class, Industry Average, or Laggard. In addition to having common performance levels, each class also shared characteristics in five key categories: (1) **process** (the approaches they take to execute daily operations); (2) **organization** (corporate focus and collaboration among stakeholders); (3) **knowledge management** (contextualizing data and exposing it to key stakeholders); (4) **technology** (the selection of the appropriate tools and the effective deployment of those tools); and (5) **performance management** (the ability of the organization to measure its results to improve its business). These characteristics (identified in Table 4) serve as a guideline for best practices, and correlate directly with Best-in-Class performance across the key metrics.

Table 4: The Competitive Framework

<table>
<tr><th></th><th>Best-in-Class</th><th>Average</th><th>Laggards</th></tr>
<tr><td rowspan="4">Process</td><td colspan="3">Standardized procedures for addressing negative audit results (payments and corrective actions)</td></tr>
<tr><td>52%</td><td>28%</td><td>25%</td></tr>
<tr><td colspan="3">Automated workflow from tax preparation to remittance</td></tr>
<tr><td>46%</td><td>30%</td><td>13%</td></tr>
<tr><td rowspan="4">Organization</td><td colspan="3">Accounting staff oversees the adherence to taxation processes and regulations</td></tr>
<tr><td>78%</td><td>54%</td><td>44%</td></tr>
<tr><td colspan="3">Training programs in place to ensure adoption of proper sales and use tax management protocols</td></tr>
<tr><td>56%</td><td>34%</td><td>25%</td></tr>
<tr><td rowspan="4">Knowledge Management</td><td colspan="3">Automated sales and use tax rate updates</td></tr>
<tr><td>58%</td><td>47%</td><td>35%</td></tr>
<tr><td colspan="3">Database for logging / archiving tax transaction history and maintaining audit trails</td></tr>
<tr><td>68%</td><td>46%</td><td>24%</td></tr>
<tr><td rowspan="2">Technology</td><td colspan="3">Sales and use tax management technologies in use:</td></tr>
<tr><td>▪ 77% tax rate calculation solutions
▪ 73% sales and use tax preparation solutions
▪ 74% sales and use tax filing solutions
▪ 42% tax exemption certificate / exception management solutions</td><td>▪ 64% tax rate calculation solutions
▪ 45% sales and use tax preparation solutions
▪ 46% sales and use tax filing solutions
▪ 23% tax exemption certificate / exception management solutions</td><td>▪ 31% tax rate calculation solutions
▪ 31% sales and use tax preparation solutions
▪ 31% sales and use tax filing solutions
▪ 6% tax exemption certificate / exception management solutions</td></tr>
</table>

	Best-in-Class	Average	Laggards
Technology (continued)	Sales and use tax management technologies in use:		
	▪ 63% tax remittance tools ▪ 45% audit control solutions ▪ 60% ERP systems with sales and use tax module ▪ 76% accounting software	▪ 45% tax remittance tools ▪ 17% audit control solutions ▪ 41% ERP systems with sales and use tax module ▪ 64% accounting software	▪ 25% tax remittance tools ▪ 13% audit control solutions ▪ 29% ERP systems with sales and use tax module ▪ 50% accounting software
Performance	Costs associated with negative audit results (fines / penalties / corrective labor) are consistently tracked		
	64%	48%	6%
	Tax overpayments are consistently tracked		
	56%	49%	18%

Source: Aberdeen Group, May 2011

Capabilities and Enablers

Based on the findings of the Competitive Framework and interviews with end-users, Aberdeen's analysis of the Best-in-Class reveals that to effectively manage sales and use taxes, companies need to provide the necessary tools to their stakeholders to gain visibility to a dynamic regulatory environment, and / or enable process automation to reduce calculation errors.

"Automation of sales and use tax management processes is increasingly being used to manage our compliance needs and we see this trend catching on in the future, as auditors are transitioning to more sophisticated auditing techniques."

~ General Manager,
Tax Management, PwC

Process

In addition to having standardized procedures in place to manage tax workflow and information, organizations are looking at standardizing procedures for addressing audits. Best-in-Class companies are nearly 42% more likely than all other companies to:

- Have a process for communicating with the local government during audits
- Have a method of addressing negative audit results
- Have a process for establishing data transparency with auditors

Companies with nexus in numerous jurisdictions, including multi-national organizations that deal with VAT have a larger stake in audit exposure by multiple government entities. To mitigate this elevated risk, particularly in light of a distributed / disparate set of employees, a common set of procedures need to be implemented to address internal tax management and external tax pressures. With competitive forces driving many companies to expand into new sales territories, it is in their best interest to provide good impressions to local jurisdictions that grant them rights to do business thereabouts.

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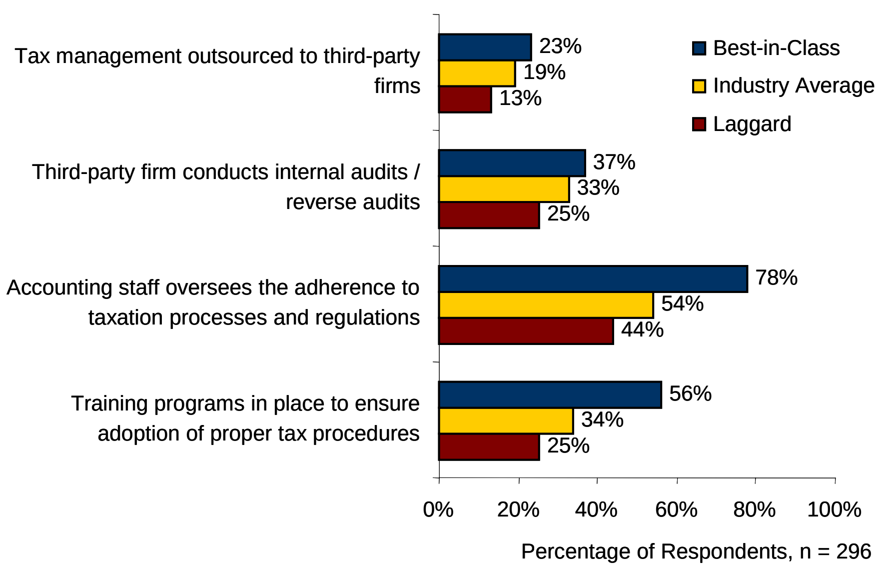
Fax: 617 723 7897

Organization

It is safe to say that with any major corporate initiative, the first step towards success is attaining executive support. In sales and use tax management, the responsibility lies predominantly with CFOs, finance VPs / directors, and / or controllers in small- and mid-sized organizations. Whereas the same responsibility lies with tax directors / managers in large organizations, where dedicated resources are more economically feasible; most executives recognize the need to reduce audit exposure in their tax and accounting departments, and are constantly evaluating how to best align their staff expertise with tax compliance requirements. That said, Best-in-Class executives take the alignment a step further by encouraging feedback from their staff members on what works best. They seek all options, including staff training, software implementation, or augmenting their tax management team to include third-party experts. This constant feedback and resource management process is what enables Best-in-Class companies to outperform their competitors. Figure 3 depicts the level of organizational involvement around sales and use tax management among the Best-in-Class.

Figure 3: Organizational Involvement among the Best-in-Class



Source: Aberdeen Group, May 2011

Knowledge Management

Part of offering transparency externally to government auditors, and internally among the tax staff, is the need to possess a robust database (a centralized repository) of tax rates, regulations, exemptions, and transaction records / audit trail. Decisions and corresponding actions are only as good as the information used to make them. Having the real-time capability to store, share, and change tax information becomes the key to increasing transaction accuracy and reducing audit risk. Employee turnover in organizations has always been a concern for executives. Losing one or two

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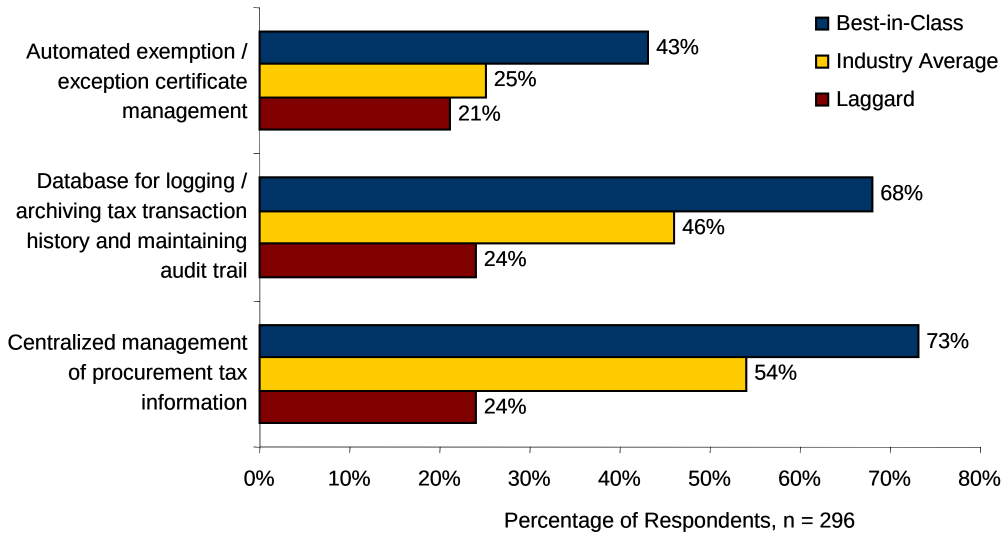
Fax: 617 723 7897

residential tax experts within a company can prove to be quite disruptive to workflow. Having an effective knowledge management system in place can mitigate this risk by providing the necessary support during such staff transitions and / or losses. Figure 4 depicts the current knowledge management capabilities possessed by the Best-in-Class.

Figure 4: Knowledge Management among the Best-in-Class

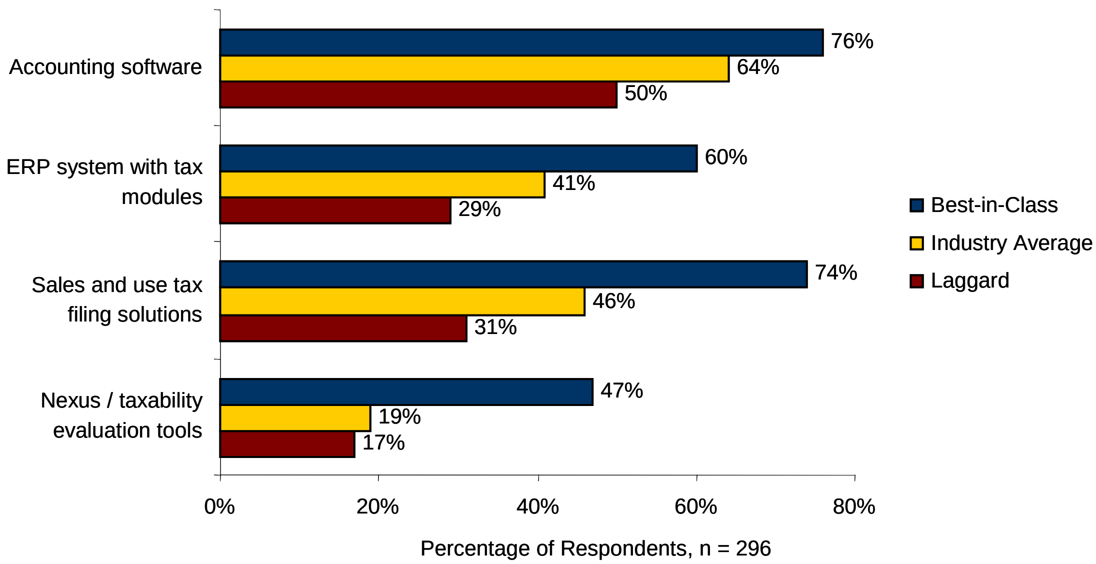


Source: Aberdeen Group, May 2011

Technology

In a dynamic regulatory environment, where tax rate changes are numerous and frequent, it becomes apparent that human capabilities are at a disadvantage over software automation. Working in all global time zones around the clock, technology has enabled the capture and use of dynamic tax rates to increase corporate productivity. This increase in efficiency can be viewed in terms of staff roles. With regard to billing tax and procurement tax, sales staff can now focus on selling, and buyers and focus on buying. Saving hours of hands-on tax rate research among their staff, companies can effectively minimize resource costs and manually-induced errors. Figure 5 depicts the technologies most used by companies in support of sales and use tax initiatives.

Figure 5: Technologies Used to Support Sales and Use Tax Management

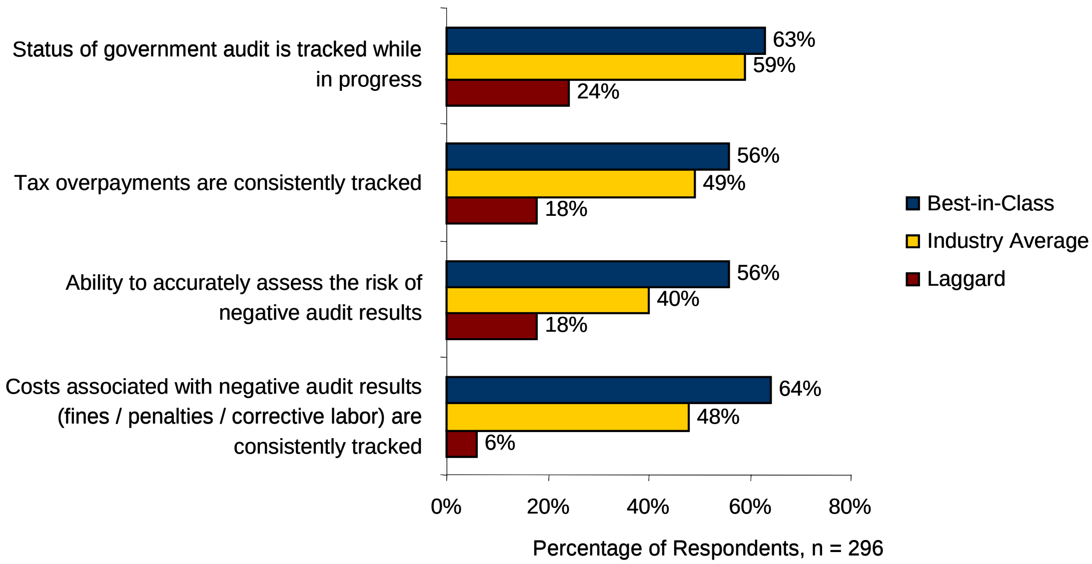


Source: Aberdeen Group, May 2011

Performance Management

Before a company makes an investment, it evaluates the potential Return on Investment (ROI). This is the case in many corporate initiatives, but particularly important in tax management. Why? Most investments in professional services and / or software are geared only towards reducing cost, and increasing top-line revenue. With tax management, it is about reducing cost, reducing risk, maintaining compliance, increasing staff productivity - and by adding all these factors together, a company effectively increases the bottom-line profit. That said, to evaluate the success of a tax management initiative and its ROI, a series of performance measurements must be implemented to compare the initiative's before-and-after levels of: audit penalties / fines and corrective labor costs, audit exposure / risk, and overpayment. Figure 6 depicts the importance of tracking performance by the Best-in-Class.

Figure 6: Performance Tracking by the Best-in-Class



Source: Aberdeen Group, May 2011

Aberdeen Insights — Technology: SaaS Deployments

As an effort to save on hardware procurement and maintenance costs, companies are looking into using Software-as-a-Service (SaaS) deployments to support their tax management requirements. By using this remote service, where the tax engine is being hosted by its vendor, companies essentially outsource their tax management responsibility to a technology entity - where a dynamic database of tax rates constantly ensures accurate tax calculations for sales transactions across various states, regions, and / or jurisdictions. Some SaaS tax solution providers also have e-commerce support capabilities as well, where tax calculations are integrated seamlessly with online checkout systems.

In terms of technology deployment methodologies among organizations, Aberdeen's current study reveals that 18% of companies are implementing SaaS tax solutions, while the majority are still deploying their tax solutions on-premise. Of the 18% of SaaS users, 33% of them achieved Best-in-Class status per the key performance indicators outlined in Table 1, and 73% of them have annual revenues of $50 million or less (the threshold that Aberdeen uses to define small companies). That said, despite larger enterprises with robust ERP platforms that accommodate tax management solutions, small companies with smaller budgets are finding ways to align their taxation processes with cost-effective technologies to achieve success.

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Fax: 617 723 7897

Chapter Three: Required Actions

The data in the prior two chapters have revealed that companies with proper processes and tools in place are realizing greater success with their tax management initiatives. Visibility into tax data and information is not just critical internally for proper calculation, filing, and remittance, but also important externally for government audits. Whether a company is trying to move its performance in sales and use tax management from Laggard to Industry Average, or Industry Average to Best-in-Class, the following actions will help spur the necessary performance improvements:

Laggard Steps to Success

- **Automate workflow from tax preparation to remittance** (13% of Laggards currently have such system in place, compared to 30% of the Industry Average). Aggregating all the tax collections from customers and ensuring that all the numbers are accurately reported can be a daunting task. By having a system in place where people, process, and tools all work in unison enables the exact tax amount collected to be transcribed directly to the tax forms (with minimal manual re-entry), and that the right personnel transmits this information to the payment department to ensure timely remittance to the state and local government(s). By establishing this workflow system, Laggards reduce the risk of remittance delay, and the cost of erroneous filings.
- **Maintain a database or centralized repository of tax transaction history and audit trail** (24% of Laggards currently have such platforms in place, compared to 46% of the Industry Average). As with many review and evaluation exercises, government audit can be prone to error. Companies must empower themselves during times of audit by making transaction data transparent to auditors to ensure an accurate evaluation, and earn the trust of auditors to reduce the chances of future audits. Additionally, by having a streamlined audit preparation and support procedure in place, future audits can be expedited. By keeping good documentation of tax transactions, Laggards effectively decrease their audit exposure.

Industry Average Steps to Success

- **Leverage tax domain expertise to ensure compliance** (54% of the Industry Average currently have such initiatives in place, compared to 78% of the Best-in-Class). Companies should continue to evaluate the level of tax domain expertise available in house (whether it resides in the accounting department, or wholly within the tax department), and seek external tax consulting services if internal resources fall short of the requirement. Having a team of

Fast Facts

√ 44% of the Best-in-Class companies integrate / streamline their tax management processes from preparation through remittance

√ 77% of the Best-in-Class companies have tax rate calculation solutions in place

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external tax professionals could also add a layer of liability protection between the organization and the government auditors - often times, these seasoned tax consultants possess the knowledge of local tax requirements that corporate tax staff are not privy to when expanding into new regions. During times of government inquiry, these consultants can also assist in providing audit support. By ensuring access to tax experts, Industry Average companies can improve their compliance standings.

- **Standardize procedures for addressing negative audit results** (28% of the Industry Average currently have such processes in place, compared to 52% of the Best-in-Class). Often times, companies are left in a state of panic when faced with a government audit. What's worse is not being able to effectively address fines, penalties, or corrective actions when found at fault after an audit. Companies should leverage tax experts, or the support of tax software solution providers, to ensure audit accuracy to start. This also give the company an opportunity to evaluate what went wrong, so it can re-engineering current processes to eliminate or reduce future faults. By having a protocol to handing government audits, as it is happening, and to address potentially negative audit results, as it has been determined, Industry Average companies can reduce the cost and time associated with the entire audit process.

Best-in-Class Steps to Success

- **Automate tax rate updates to facilitate calculations.** While 58% of the Best-in-Class have tax automation capabilities in place, and 87% of them are more likely than all other companies to streamline tax operations, adoption rates are still relatively low, indicating that there are still challenges to overcome in terms of technology integration and interoperability, as well as process training. These top-performing companies are growing steadily to include new sales territories and supplier relationships each day. With more responsibilities ahead to comply with the multitude of dynamic tax rates, Best-in-Class companies need to continue to leverage automated tax calculation engines, electronic filing and remittance tools, and audit management solutions to stay competitive.

"Automation of sales and use tax management has significantly reduced the strain on resources in tax form preparation and reporting."

~ Manager, Operations,
Navico Inc.

- **Establish training programs to ensure the adoption of proper tax procedures** While 56% of the Best-in-Class currently have these programs in place, the marketplace still faces a conundrum - corporate income tax management is still being viewed as being more critical than sales and use tax management. As revealed earlier in the report, the percentage of government revenue attributed to sales and use tax is growing, and so will the audits around it. It is imperative that companies educate its financial staff the potential impact of repeated audits - with fines and penalties that can cut into the corporate bottom line. By bringing awareness (and urgency) to the importance of effective sales and use tax management, Best-in-Class companies can reduce their overall corporate risk profile, and ensure continuity in the region / jurisdiction that they are doing business in.

Aberdeen Insights — Summary

Many companies only seek professional tax assistance during times of audit. What is apparent is the amount of due diligence and government communication that these tax consulting firms must perform to ensure compliance. The hours spent on corrective actions are often greater than those invested in preventative actions. The lesson here is that being proactive, systematic, and judicious in improving sales and use tax management pays greater dividends than being reactive to audit situations. Many tax consulting firms recognize this, and have been deploying client training programs as part of their audit management support. Successful firms further add client value by recommending and, in most cases, deploying tax software to assist in the compliance process. As a client company, it is important to work with a firm that recommends process re-engineering and software adoption based on alignment to a client's tax management objectives - and not on preferred-software status and / or application interoperability criteria.

From the data gathered for this report, Best-in-Class companies demonstrate that having tax domain experts alone to execute on tax management initiatives is simply not enough to yield success. These companies rely on process and workflow automation to ensure compliance with state / local / jurisdictional tax requirements. To achieve this level of efficiency, Best-in-Class companies leverage internal and external experts to ensure proper technology integration and adoption. As a result, they build a strong alignment between domain expertise and compliance measures that allow significant reduction in corporate risk profile.

Telephone: 617 854 5200
Fax: 617 723 7897

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Appendix A: Research Methodology

Between April and May 2011, Aberdeen examined the use, the experiences, and the intentions of nearly 300 companies using Sales and Use Tax (SUT) solutions and services in a diverse set of industries.

Aberdeen supplemented this online survey effort with interviews with select survey respondents, gathering additional information on tax management strategies, experiences, and results.

Responding organizations included the following:

- *Job title:* The research sample included respondents with the following job titles: CEO / President (22%); CFO / CIO (8%); EVP / SVP / VP (7%); GM / Managing Director (4%); Partner / Principal (4%); Controller (6%); Tax Director (11%); Tax Manager (26%); Accounting Staff (7%); Consultant (4%); and other (1%).
- *Department / function:* The research sample included respondents from the following departments or functions: tax management (28%); corporate management (16%); business development / sales (11%); finance / administration (10%); accounting (9%); information technology (6%); operations (4%); logistics / supply chain (3%); procurement / purchasing (3%); manufacturing / production (2%); marketing (2%); and other (6%)
- *Industry:* The research sample included respondents mostly from wholesale / distribution (11%) industry.
- *Geography:* The majority of respondents (88%) were from North America. Remaining respondents were from the Asia-Pacific region (5%), Europe (4%), Middle East & Africa (2%) and South / Central America and Caribbean (1%).
- *Company size:* Twenty-five percent (25%) of respondents were from large enterprises (annual revenues above USD $1 billion); 27% were from midsize enterprises (annual revenues between USD $50 million and USD $1 billion); and 48% of respondents were from small businesses (annual revenues of USD $50 million or less).
- *Headcount:* Thirty-nine percent (39%) of respondents were from large enterprises (headcount greater than 1,000 employees); 29% were from midsize enterprises (headcount between 100 and 999 employees); and 32% of respondents were from small businesses (headcount between 1 and 99 employees).

Study Focus

Responding tax and accounting executives completed an online survey that included questions designed to determine the following:

√ The degree to which sales and use tax solutions is deployed in their billing and procurement operations, and the compliance benefits of the technology

√ The structure and effectiveness of existing sales and use tax processes and procedures

√ Current and planned use of tax management solutions to reduce audit exposure and risk

√ Current and planned use of third-party tax firms to conduct internal / reverse audits, manage government audits, and outsource tax management responsibilities

The study aimed to identify best practices for effective sales and use tax management across various industries, and to provide a framework by which readers could assess their own tax management capabilities.

Table 5: The PACE Framework Key

Overview
Aberdeen applies a methodology to benchmark research that evaluates the business pressures, actions, capabilities, and enablers (PACE) that indicate corporate behavior in specific business processes. These terms are defined as follows: **Pressures —** external forces that impact an organization's market position, competitiveness, or business operations (e.g., economic, political and regulatory, technology, changing customer preferences, competitive) **Actions —** the strategic approaches that an organization takes in response to industry pressures (e.g., align the corporate business model to leverage industry opportunities, such as product / service strategy, target markets, financial strategy, go-to-market, and sales strategy) **Capabilities —** the business process competencies required to execute corporate strategy (e.g., skilled people, brand, market positioning, viable products / services, ecosystem partners, financing) **Enablers —** the key functionality of technology solutions required to support the organization's enabling business practices (e.g., development platform, applications, network connectivity, user interface, training and support, partner interfaces, data cleansing, and management)

Source: Aberdeen Group, May 2011

Table 6: The Competitive Framework Key

Overview	
The Aberdeen Competitive Framework defines enterprises as falling into one of the following three levels of practices and performance: **Best-in-Class (20%) —** Practices that are the best currently being employed and are significantly superior to the Industry Average, and result in the top industry performance. **Industry Average (50%) —** Practices that represent the average or norm, and result in average industry performance. **Laggards (30%) —** Practices that are significantly behind the average of the industry, and result in below average performance.	In the following categories: **Process —** What is the scope of process standardization? What is the efficiency and effectiveness of this process? **Organization —** How is your company currently organized to manage and optimize this particular process? **Knowledge —** What visibility do you have into key data and intelligence required to manage this process? **Technology —** What level of automation have you used to support this process? How is this automation integrated and aligned? **Performance —** What do you measure? How frequently? What's your actual performance?

Source: Aberdeen Group, May 2011

Table 7: The Relationship Between PACE and the Competitive Framework

PACE and the Competitive Framework – How They Interact
Aberdeen research indicates that companies that identify the most influential pressures and take the most transformational and effective actions are most likely to achieve superior performance. The level of competitive performance that a company achieves is strongly determined by the PACE choices that they make and how well they execute those decisions.

Source: Aberdeen Group, May 2011

Appendix B:
Related Aberdeen Research

Related Aberdeen research that forms a companion or reference to this report includes:

- *Managing Value-Added Tax (VAT) in a Global Environment*; January 2011
- *Effective Sales and Use Tax Management: Reducing Errors and Increasing Productivity* ; May 2010

Information on these and any other Aberdeen publications can be found at www.aberdeen.com.

Author: William Jan, Senior Analyst, Financial Management & GRC, (william.jan@aberdeen.com)