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cutting through complexity

TAX

Good, Better, Best

The race to set standards
in global tax management

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Contents

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.

Summary of key findings & insights – what's changed?

KPMG International's series of global benchmarking studies have charted the evolution of tax departments since 2006. Our 2009 study showed that the tax departments that add the most value to their companies are also the ones that paid most attention to three key areas in conducting their daily activities:

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

In 2009, we called this getting the basics right. So, with the current survey, we were keen to see how tax departments have progressed in these areas, especially given ongoing economic uncertainty and continuing regulatory reform.

Based on our analysis of the 2012 survey results and differences from the results in 2009, we found that tax departments are markedly improving in the area of accountability and making some strides forward on standardization and efficiency. However, tax departments still seem to have much more work to do on increasing their connectivity, integration and alignment with other functions.

Here, we summarize the most important findings and insights from the survey. A wealth of additional data and analysis — including supplementary reports for the countries in the survey — is available at www.kpmg.com/goodbetterbest.

Improving accountability

- Tax departments are making good progress in adopting company-wide tax strategies. Survey results show that boards and corporate leadership are taking more interest in, and responsibility for, tax matters, and getting more involved in guiding tax strategy.
- Respondents report a relatively high degree of focus on setting measurable performance indicators. Compliance-related indicators are by far the most prevalent. In line with this, accurate and timely tax return compliance remains the most important activity for tax departments, topping their strategic priorities and occupying more of their time than other activities. Respondents say that, in aggregate, more than half of their tax departments' time is spent on compliance, reporting and managing tax audits.

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

77%
of tax department strategies are board-approved

Over 3/4
of respondents have performance measures related to reporting and/or compliance

- There is a clear trend toward centralizing resources within a global or company-wide tax department that directs or manages the global tax function. The number of respondents who report having employees with tax responsibilities for particular regions or multiple countries rose significantly since 2009. The majority of these employees report directly to the headquarters tax department.

Making headway on standardization

- Survey results show that companies are taking action to improve tax processes and controls by standardizing activities and systems.
- Respondents express satisfaction with current levels of investment in tax technology and process improvement. The majority of respondents have projects in progress in these and other areas such as better training for tax staff and tax strategy and operational reviews.
- Respondents report a high degree of standardization of processes and controls, particularly for compliance-related activities. Respondents' finance functions are also actively engaging in transformation initiatives, but tax departments usually are not integrally involved.
- Only a minority of respondents say their companies use cloud computing. An even smaller group use the cloud for storing accounting or transactional data, preventing tax departments from using cloud storage for its benefit. It seems that the tax implications of cloud computing have not been thoroughly reviewed by those companies that use cloud computing, which suggests that the tax department's involvement in cloud projects is limited.

Room for improvement on connectivity

- With tax departments devoting much of their attention to compliance, less time and attention are being spent on more forward-looking, higher-value activities.
- In terms of how the tax department is measured and where time is expected to be spent over the next 12 months, the lowest-ranking priorities are integration with business groups and early indication of routine transactions, cash tax planning, and tax process improvement.
- For tax departments that will restructure in the near future, "cost reduction" is the reason with the greatest increase since 2009. Better alignment with the business or finance function is the least common reason.

76%
of respondents now have a headquarters tax department

62%
of tax departments are engaged in or considering overall tax strategy and operational reviews

Under 40%
are "integrally involved" in finance function transformation initiatives

Only 1/3
of time is expected to be spent on effective tax rate optimization, cash tax planning, process improvement and integrating with the broader business

The challenges ahead

- Tax controversy has been increasing sharply since 2009, with respondents reporting higher controversy activity in all taxation areas. Respondents say that tax authorities are taking more interest in how well tax departments are managed, for example, by scrutinizing tax and accounting processes and controls, tax strategy and risk management, and technology.
- We expect this trend to continue as more tax authorities take up horizontal monitoring and risk-based tax audit techniques. Regulatory changes, such as the US Dodd-Frank Act and the EU country-by-country tax reporting proposals, will add even more pressure on companies' ability to meet their tax compliance and reporting burdens.
- Tax directors are satisfied with their existing administrative budgets, staffing levels, and investments in technology and process improvement. Given the challenges ahead, corporate and tax leadership will likely want to reconsider whether satisfaction with the adequacy of tax resources and investment is warranted.

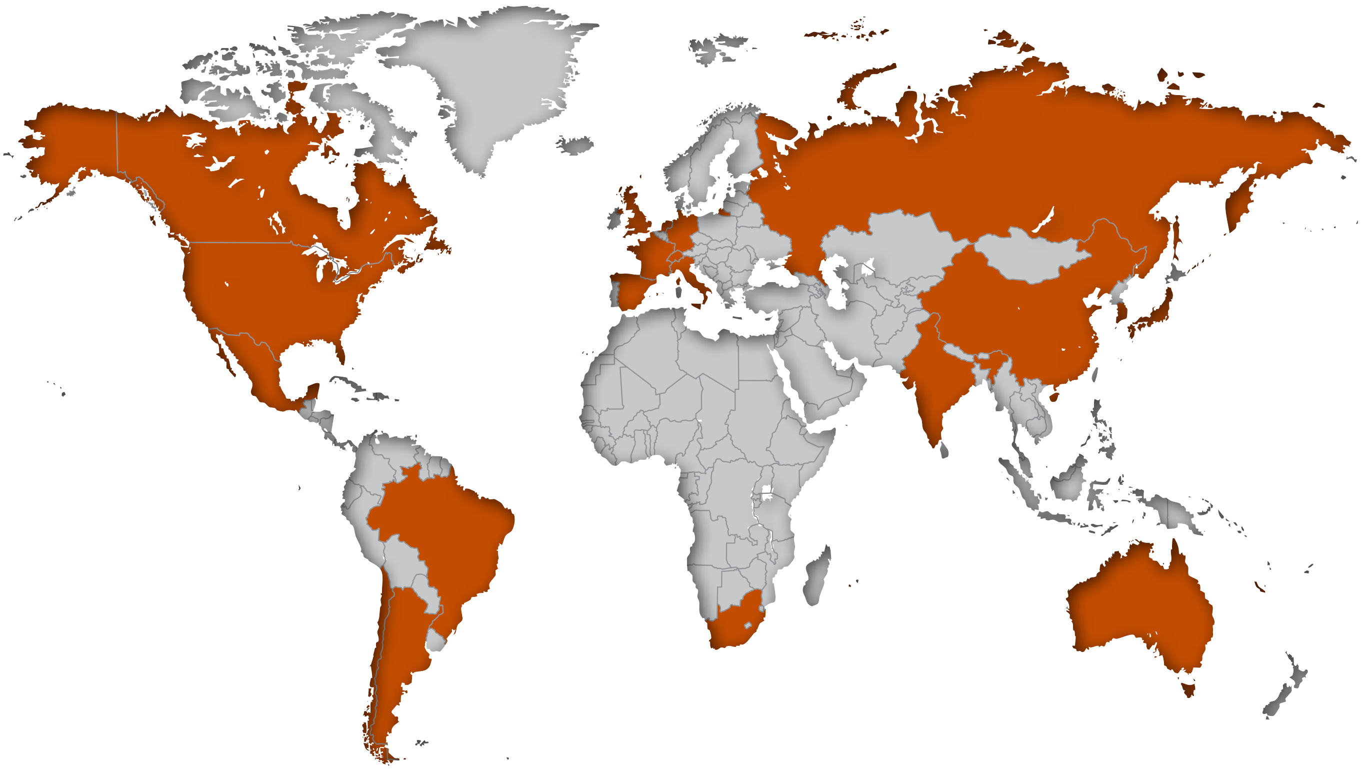
In summary, the survey reveals that forward-thinking tax directors face a difficult dilemma: as tax compliance burdens and disputes continue to mount, their departments will meet greater challenges in managing these obligations while improving their performance and focusing on the more value-adding aspects of the tax department's role.

Given this dilemma, this current survey shows that the lessons of our 2009 report — that transforming the performance of the tax department requires getting accountability, standardization and connectivity right — are now even more important.

2/3
of tax departments are currently involved in tax controversy

Over 1/2
of respondents say tax authorities have become more focused on tax and accounting processes and controls, tax strategy and risk management, and technology in the last 12 months

79%
of respondents are satisfied with their tax department's administrative budgets



COUNTRY	BASE SIZE
Argentina	50
Australia	50
Brazil	50
Canada	50
Chile	50
China	50
France	50
Germany	50
Hong Kong	50
India	50
Italy	50
Japan	50
Mexico	50
Netherlands	50
Russia	50
Singapore	50
South Africa	50
South Korea	50
Spain	50
Switzerland	50
United Kingdom (UK)	50
United States (US)	100
TOTAL	1150

About the survey

- KPMG International's global survey of people in charge of tax policy and operations of companies 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 (50 respondents in 21 countries and 100 in the US) took part in blind telephone surveys to share their opinions on how tax departments are adapting to current challenges. About 700 of respondent companies are Fortune 500, Forbes 2000 or equivalent.
- 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.

Source: KPMG International 2012

Enabling the tax department of the future

The most effective, highly valued tax departments are those that manage tax risk while identifying improvement opportunities through core tax management skills and proactive collaboration with all parts of the business.

Since 2006, KPMG International's member firms have monitored the evolution of tax departments through a series of benchmarking surveys of those responsible for the tax department around the globe. Our 2009 research, validated by the experience of KPMG member firms working with some of the world's leading companies, suggested that the highest performing tax departments are also those that focus on getting the basics right in three key areas:

1. **improving accountability** to clarify the tax department's roles and responsibilities within the context of a company-wide, board-approved tax governance framework;

2. **improving standardization** to automate and strengthen tax processes and controls and ensure all tax compliance obligations are met; and

3. **improving connectivity** between the tax department and other business areas so they work together as proactive partners in setting and advancing business objectives.

The focus on these areas makes intuitive sense. Clear accountabilities can ensure that the tax department strategy is aligning with and supporting the wider company or enterprise strategy and that their goals and performance measures are agreed upon with key stakeholders. Standardization of processes and technology improves consistency, quality and efficiency, allowing tax teams to spend less time on compliance and more on value-adding pursuits. Connectivity and participation with all parts of the company — from boards and senior leaders to other functions such as Finance, Treasury, M&A, Marketing, IT, HR, Sales and Procurement — are key to ensuring tax affairs are well managed and boost the tax department's value, profile and influence.

Our analysis of the 2012 survey results discusses the progress of tax departments in these three areas. The findings show that they are making progress in improving accountability and standardization but have more work to do in connectivity.

In the final section of this report, we identify the key threat to progress: the rising compliance and audit burden, which risks attracting more time and resources away from value-adding activities. We ask whether the challenges can turn into opportunities. Without substantial improvements in getting the basics right, how can the leading tax department of the future manage compliance responsibilities and be the proactive business partner its colleagues need?

Improving accountability – vertical alignment strengthens

Our previous surveys charted the rising importance of the corporate governance of tax as companies faced growing pressure from a range of parties internally and externally to demonstrate that they are well-run, responsible organizations. It is now probably fair to say that the management of tax is one of the key criteria by which corporate governance is judged by investors and other third-parties, such as regulators, analysts and the media.

The world's tax authorities are showing much greater interest in evaluating how a company's tax matters are governed. For example, current tax authority risk assessment programs in the UK, Australia and the Netherlands explicitly address the strength of a company's tax governance policies.

Tax authorities are also demanding more transparency in compliance processes. For example, in the UK, senior accounting officers of large companies must annually certify that their tax systems and controls are adequate. The US requires companies to report the impact of "uncertain tax positions" on their balance sheets and tax returns. Using these disclosures, tax authorities will focus on areas of potential non-compliance or differing interpretation, with the expectation of resolving disputes and settling tax assessments more efficiently.

Other regulators and non-governmental organizations are also looking at how a company's approach to tax management is helping fulfill what are seen as its wider corporate responsibilities. For example, reporting requirements under the Dodd-Frank Act in the US and the proposed EU Transparency Directive will require detailed country-by-country (or project-by-project in some cases) tax data. A company's own need for timely and accurate financial data is also challenging the tax department to think more widely about what its responsibilities entail and how to fulfill them.

Since our last survey in 2009, boards and finance executives are clearly responding to this rising focus on the management of tax. The current survey shows senior executives and directors are taking more interest in, and responsibility for, tax matters.

Which of the following statements are true of your company?

	2009	2012
We have a tax strategy that is consistent with our overall business strategy	84%	93%
The board has approved the tax strategy	48%	77%
Our approach to tax risk management has been approved by the board and/or corporate leadership	48%	75%
The board and/or corporate leadership has provided guidance directly to the tax department regarding the strategy	51%	73%
We have a documented approach to tax risk management	66%	71%
We have global standards related to tax policies and procedures	60%	70%
We have formally documented our tax strategy (2012 survey only)	N/A	63%

Source: KPMG International 2009, 2012

"In today's world, you need to have transparent information in a timely manner. Internally and externally, there's more and more emphasis on tax, in terms of tax transparency initiatives, total tax contribution and so on. I think the tax department will become even more important in the future."

— Tax director of a leading multinational mining company

The percentage of respondents who have a tax strategy that is consistent with their overall business strategy rose from 84 percent in 2009 to 93 percent currently. For 73 percent of respondents, the board and/or corporate leadership are directly involved in providing guidance on the tax strategy — a significant increase from 2009 (51 percent). Similarly, 77 percent of respondents report that their board has approved the tax strategy, up from 48 percent in 2009.

Smaller companies gaining more ground

Notably, respondents from smaller companies (with annual revenue less than USD500 million) report slightly better progress on areas related to tax governance and operations. In comparison to larger companies, respondents from smaller companies are more likely to have:

- a board-approved tax strategy;
- board guidance on the strategy; and
- key performance indicators (KPI) to benchmark against each of the named categories.

This suggests that boards and tax teams of smaller companies can communicate more effectively and act more quickly. Their larger counterparts can have a harder time gaining consensus and resources needed. Given the matters at stake, it is just as or even more important for tax departments of large companies to ensure clarity of accountabilities.

Routine compliance tops tax department priorities

Survey results suggest that, as in previous years, tax departments are primarily focusing on day-to-day compliance work. Accurate and timely tax return compliance is the most important activity driving tax department objectives, followed closely by accurate and timely financial reporting.

How important is each of the following in driving your tax department's overall objectives in the next year?

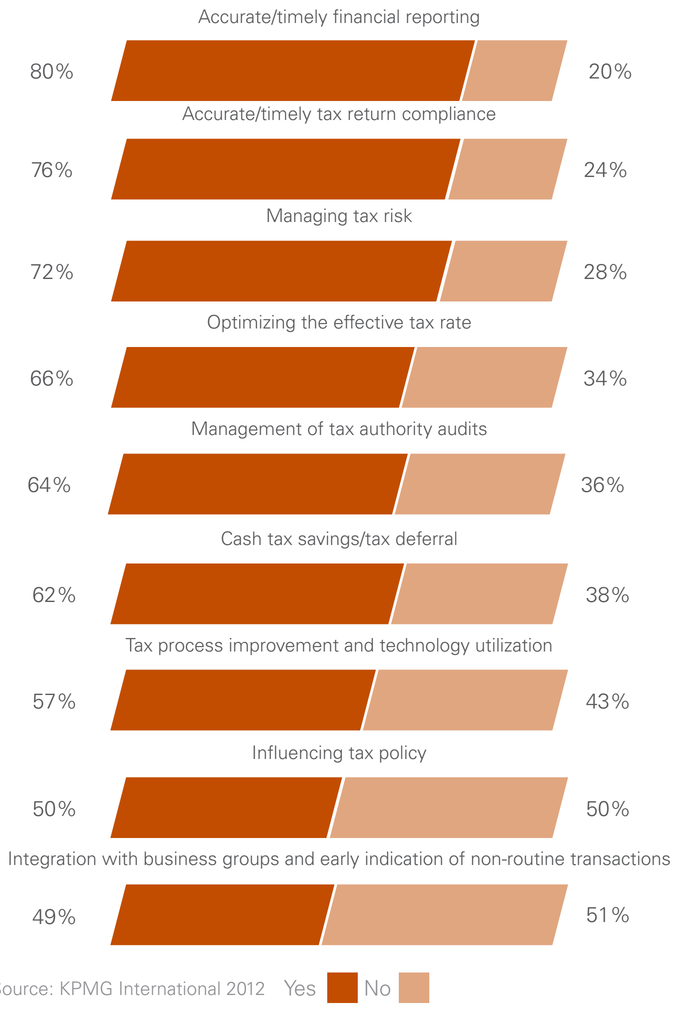
5 = extremely important; 1 = not at all important

Accurate/timely tax return compliance	4.48
Accurate/timely financial reporting	4.41
Managing tax risk	4.22
Management of tax authority audits	4.11
Optimizing the effective tax rate	4.03
Cash tax savings/tax deferral	3.88
Tax process improvement and technology utilization	3.76
Integration with business groups and early indication of non-routine transactions	3.65
Influencing tax policy	3.61

Source: KPMG International 2012

We asked a new question in the current survey to investigate the focus of the tax department on setting KPIs. Encouragingly, a high proportion of respondents report the existence of formal KPIs across a wide range of tax department activities. Consistent with the priority given to compliance and reporting, the highest degree of KPI setting relates to this activity.

Have you developed KPIs to benchmark against goals?



Source: KPMG International 2012

The percentages are lower for activities that can add value, such as process improvement and business integration. This raises the question of whether tax departments are reluctant to set KPIs in more strategic areas or whether setting reasonable benchmarks for these activities is a difficult metric to put in place.

Case study #1 – measuring tax department performance & value

On finding that its effective tax rate (ETR), as reported in the financial statements, seemed out of line, a European banking group undertook a detailed review of the components of its ETR and a benchmarking to its peer group. The review not only revealed that the reasons for the differences were justifiable but also opened more informed discussions between the tax department and the board about the true value that the tax department provided to the company.

The discussions led to the development of a balanced scorecard approach for KPIs for the tax department. The new KPIs focused not only on traditional performance measures for tax, such as ETR, but also on a range of broader measures, such as tax cash flow management of indirect taxes, speed of resolution of disputes, and talent management.

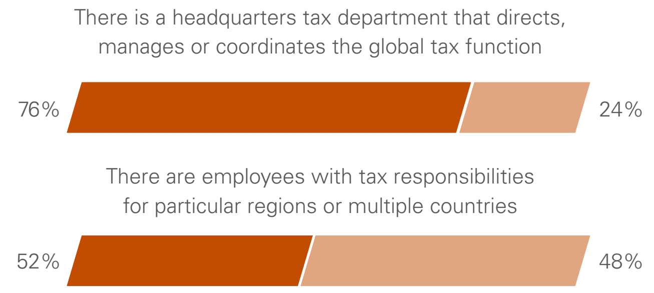
> "Our tax department KPIs address compliance first of all, making sure that all the filings and claims are made in due order. Then we're measured on the extent to which we minimize tax more broadly. We're given a realistic cash tax target and the KPI would be to try and outperform that cash tax target — and then to outperform the first target by another 10 percent."
>
> **—Tax director of a UK-based energy company**

Centralizing accountability & management

Another aspect of good tax governance is establishing a tax department structure that aligns to the company-wide strategy and includes clear reporting lines and accountabilities. Since 2009, companies have acted and are centralizing the management and structure of resources in global or business-wide headquarters tax departments. This centralization can support desired improvements in accountability, control and standardized approaches.

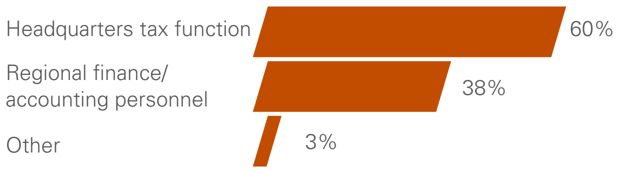
In 2009, 56 percent of respondents said that their tax department was directed, managed or coordinated from their global headquarters, compared to 76 percent currently. Additionally, the number of respondents who reported having employees with tax responsibilities for particular regions or multiple countries also rose significantly — from 29 percent in 2009 to 52 percent currently; 60 percent of these employees now report directly to the headquarters tax department. The number of respondents with employees responsible for single countries or for business units or divisions is also increasing.

Which of the following is true about your tax department structure?



Source: KPMG International 2012 Yes No

Who do they report to?



Source: KPMG International 2012

With so many challenges, the survey asked if respondents are addressing the structure of their tax department and, if so, why.

Is the structure of your tax department expected to change in the near future?

	2009	2012
Yes	16%	19%
No	84%	81%

Source: KPMG International 2009, 2012

If yes, what are the primary reasons for change?

	2009	2012
Increase/improve control	34%	65%
Reduce costs	27%	63%
Improve/create efficiencies	39%	60%
Improve/enhance tax risk management	35%	53%
Better alignment with business and/or finance function structure and needs (2012 survey only)	N/A	50%

Source: KPMG International 2009, 2012

Of the 19 percent of respondents who expect changes to their tax department's structure in the near future, 50 percent of them say that better alignment with the business and/or the finance function is among the primary reasons. However, better integration is still a lower priority in driving upcoming structural projects than improving controls, reducing costs, and improving/creating efficiencies.

Blueprint for change

The survey shows that tax directors are getting better at articulating and gaining formal approval for the tax strategy. But the current regulatory and economic environment highlights the importance of continually adapting the strategy to respond to changing circumstances. We recommend that a common purpose is agreed upon and maintained between the tax department and corporate leadership to align strategic goals and objectives.

As case study #1 shows, developing a broader set of performance measures can help quantify and communicate the full value the tax department brings to the company. We recommend defining one view of performance, shared by the tax department and corporate leadership. This includes clarifying what requirements are needed and how to measure performance.

As the tax department obtains greater clarity over these areas, the right mix of skills and team structure are essential to the execution.

"I had a lot of people sitting in a head office-type department and yet five very separate businesses. I needed to get people into the business, so I've appointed tax directors in the businesses… and scaled down the central team."

— Group taxation director of a UK-based global industrial engineering firm

Making headway on standardization - conforming global processes & controls

Our previous research identified a focus on standardization and efficiency as key characteristics of leading tax departments. Standardization eases the management of complex data flows, streamlines the performance of routine tasks and increases the accuracy of tax data and related filings. It facilitates the use of technology to monitor results and investigate anomalies. It also helps foster better understanding and communication of tax matters across the company.

2

In looking to what progress has been made in standardization and simplification of tax processes since 2009, we now find that more tax departments are actively working to make their global tax processes and controls more uniform.

The majority of respondents now rate the level of standardization of their tax controls, policies and procedures as "standardized" or "very standardized". Responsibilities and accountabilities of tax personnel are the most standardized areas. Similarly, more than half of respondents report standardization of tax compliance activities across the annual cycle — from forecasts of tax expense or ETRs and annual provision processes through to compliance and tax return processes. This, of course, leaves a sizeable minority still to reap the benefits of greater standardization. It is also worth noting that respondents say wider tax processes and technologies are the least likely to be standardized.

How would you rate the level of standardization for your tax department globally in the following areas?

5 = very standardized; 1 = not at all standardized

Responsibilities and accountabilities of tax personnel	3.84
Controls	3.69
Learning, development and career path for tax personnel	3.63
Policies and procedures	3.59
Processes	3.54
Technologies	3.43

Source: KPMG International 2012

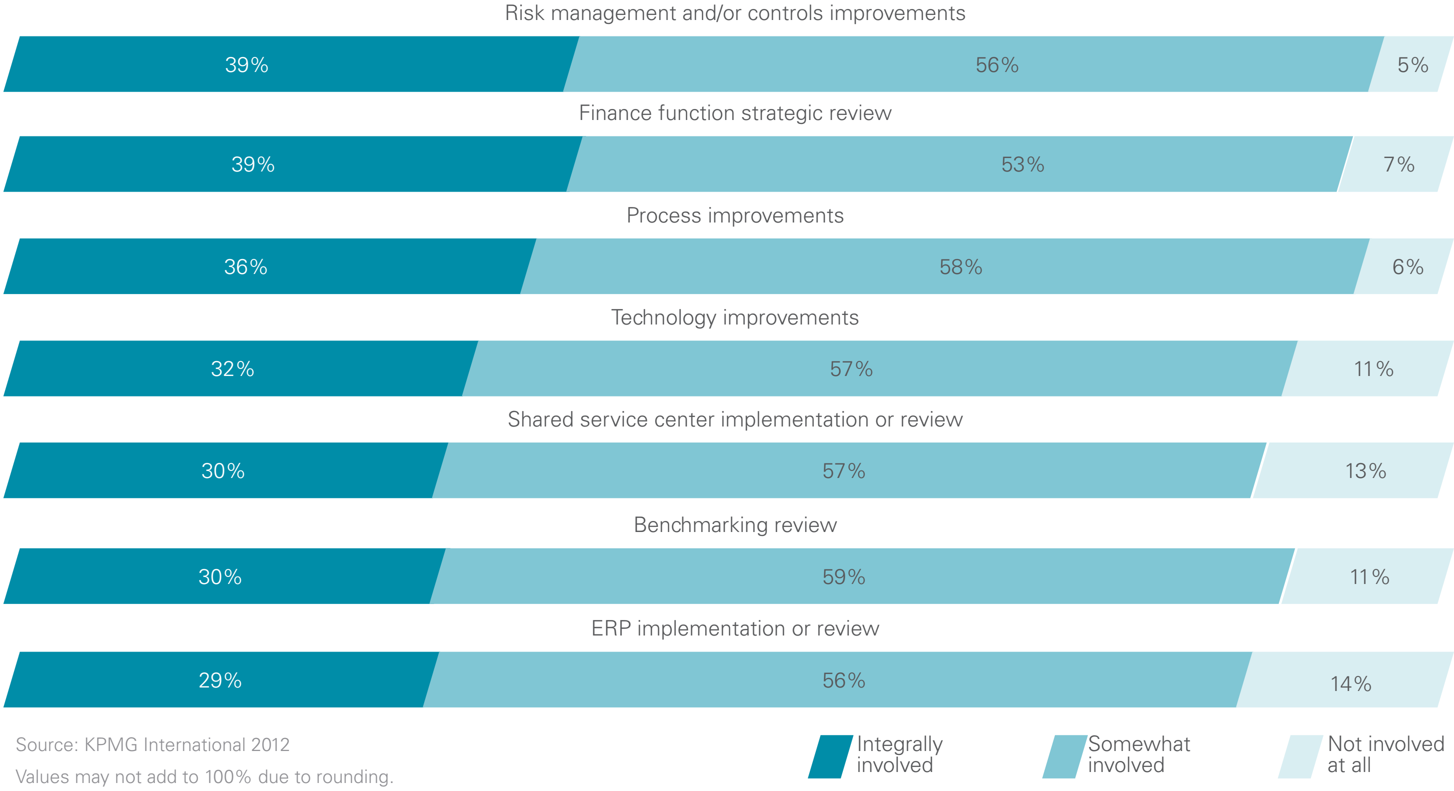
This drive for standardization is clearly gaining support: the number of respondents who say finance leadership drives standardization of their tax department strongly or relentlessly rose from 37 percent in 2009 to 51 percent in 2012. We believe this trend will continue as companies consider the performance and structure of their finance function and ask how the tax department can contribute.

Another indicator of progress in standardization is the level of investment in tax process improvement and technology. Interestingly, 74 percent of respondents in the current survey report they are satisfied with the levels of investment in tax technology and process improvement. Given that levels of standardization are lowest for tax processes and technologies, and that the majority of time is still spent on compliance and reporting, we would expect less satisfaction with current levels of investment.

In the current difficult economic, and thus investment environment, respondents may be reluctant to admit that they need more budget for projects. However, the majority of respondents say they already have projects in progress that could explain the current funding satisfaction. Whatever the reason, this level of investment focus is encouraging for the future if the amount of time on routine day-to-day activities is to be more comparable to that spent on more strategic activities.

> "One of the things that we will continue to focus on is automating the provision process to automate our transaction tax preparation."
>
> **— Tax director of a US-based communications company**

Has your company undertaken any of the following finance initiatives on a global or regional level within the past 12 months? If yes, what was your tax department's level of involvement in those initiatives?



Source: KPMG International 2012

Values may not add to 100% due to rounding.

Despite the apparent good progress in addressing standardization of tax processes and controls, there are likely to be further areas of opportunity that are not being exploited to their full extent. Among companies that report having undertaken global or regional finance transformation initiatives in the past 12 months, the tax department was "integrally involved" less than 40 percent of the time:

- 39 percent are integrally involved in risk management and/or controls improvements and finance function strategic reviews;
- 36 percent of respondents say their tax department is integrally involved in process improvements; and
- under one-third of respondents are integrally involved in technology improvement projects, shared service center implementations or reviews, benchmarking reviews and ERP reviews/implementations.

Given a tax department's typical reliance on finance function processes for a good proportion of the information they need, it is essential that tax is integrated with related finance function processes. The survey results suggest that there are still significant opportunities in pushing for efficiencies in end-to-end tax processes and for tax department involvement in enhancing the value of investment made in large business-wide initiatives. As case study #2 shows, there is now much greater understanding of how the tax department can leverage broader business developments.

Case study #2 – leveraging finance function investments

A leading international group undertook a global SAP implementation. As part of the project plan, the tax department partnered with the finance function, their tax advisers and the SAP provider to ensure that the implementation met tax compliance needs. As a result, SAP was configured to ensure that correct VAT and other indirect tax codings were properly implemented within the transactional accounting processes. Tax data was also configured to enhance compliance efficiencies when collecting and analyzing accounting data for tax return purposes.

Optimizing technology for better value

Despite opportunities, such as case study #2 illustrates, harnessing additional tax technology and process improvements is not high on the agenda for most survey respondents this year. Only 17 percent feel their level of investment in technology and tax processes is too low, down from 26 percent in 2009. About three-quarters say that their company's level of investment is "about right".

Similarly, despite the widely touted cost savings and efficiencies that cloud computing can offer, only a minority of respondents work in companies that use cloud computing. An even smaller group use the cloud for the storage of accounting or transactional data, which can limit the ability to actively use cloud storage for its potential benefits to the tax department. And only about a quarter of respondents are focusing on cloud computing's international tax implications.

To the extent that your company operates internationally, where do you focus on the implications of cloud computing?

Do not use cloud computing	62%
Transfer pricing with respect to related-party cloud payments	26%
Server location and permanent establishment issues	23%
Impact of indirect taxes (e.g. VAT/GST) on cloud payments	22%
Foreign country income characterization of outbound cloud payments	19%

Source: KPMG International 2012

Given the importance of compliance — as respondents suggest — the lack of interest in greater investment in tax technology and process improvement is unexpected. For forward-thinking tax departments, there is a strong business case for more investment in tax technology-related improvements. Indeed, automation and standardization can streamline compliance tasks while improving accuracy by:

- easing the preparation of tax provisions and year end tax reporting by standardizing local data and creating better audit trails;
- providing greater visibility of tax activity in real time and better strategic understanding of tax in the business as a whole; and
- having a central platform for managing complex international tax issues, such as a company's transfer pricing, employee relocations, and indirect tax obligations.

When technology plays a greater role in the completion of tasks, tax departments can devote more time and attention to important strategic pursuits.

Case study #3 – using technology to free up time

A global telecommunications company needed to prioritize its tax department's workload. Initially, the company focused on outsourcing their compliance needs, but this was not their preferred option. However, further investigation of the reasons for the tax department's excessive workload revealed that 70 to 80 percent of the time in preparing tax returns was spent on preliminary work that involved extracting, formatting and understanding accounting data before any tax technical analysis began.

By gaining a better understanding of the nature of the data housed within the company's accounting system and how to access it, and by coupling this with appropriate mapping and analysis technology, the company was able to cut the amount of preliminary work almost in half. This enabled the tax department to keep its compliance work in-house while maintaining its ability to deliver on other priorities.

Outsourcing tax responsibilities

Outsourcing remains a valuable option for the tax department when considering its global responsibilities. Outsourcing is often used strategically to free up in-house resources for other activities and to access best practices and investments in people, processes and technology that cannot be developed in-house.

The number of respondents that outsource or co-source tax department activities has dropped significantly, from 52 percent in 2009 to 34 percent in 2012. At the same time, use of shared service centers rose from 22 percent to 30 percent. These results are surprising, given our experience that demand for outsourced tax services is still strong. Nevertheless, the results suggest that many companies are responding to pressure to reduce costs by outsourcing less.

Which of the following, if any, do you use to carry out or support tax department reponsibilities?

	2009	2012
Outsourcing/co-sourcing	52%	34%
Finance or accounting shared service center	22%*	30%
Other finance resource	22%	25%

Source: KPMG International 2009, 2012

* In the 2009 survey, the question only referred to accounting shared service centers

Indeed, the one-third of companies that do outsource say that they have significantly increased the scope of work done by third parties since 2009. Corporate income tax compliance (which rose from 45 percent in 2009 to 69 percent in 2012) and tax controversy support (which rose from 38 percent to 66 percent) are the most commonly outsourced/co-sourced tax activities. Tax planning and business support (which rose from 34 percent to 58 percent) are not far behind.

Outsourcing/co-sourcing of work in all categories climbed between 20 and 30 percent. This suggests that these tax directors are becoming more comfortable with outsourcing and they are now better at identifying how and when outsourcing/co-sourcing can help optimize their tax operations. In the future, the majority of these respondents say the amount of work outsourced/co-sourced will remain about the same.

When deciding what tax department activities to outsource or co-source, respondents rank improved management of and visibility over compliance activities and access to technology as the most important factors to consider, alongside the expected lack of internal resources. When deciding what activities to keep in-house, knowledge retention and the proprietary or business-critical nature of the work are at the top of the list.

While outsourcing still serves its traditional role as a substitute for unavailable in-house resources, our experience is that many leading companies now consider a global or regional approach to outsourcing of compliance activities (including both tax and statutory accounting responsibilities) as a key strategic lever, as case study #4 shows.

What tax functions do you currently outsource/co-source?

	2009	2012
Corporate income tax compliance	45%	69%
Tax controversy support	38%	66%
Tax planning and business support	34%	58%
Overseas corporate income tax compliance	32%	51%
Indirect tax compliance	26%	50%
Corporate income tax provision	18%	47%
Statutory accounting/reporting preparation	20%	46%
Payroll compliance (2012 survey only)	N/A	44%
Expatriate/personnel tax compliance	25%	38%
Overseas income tax provision	17%	36%

Source: KPMG International 2009, 2012

Case study #4 – a transformative approach to compliance sourcing

After grouping its financial accounting activities into three shared service centers globally, a Fortune 500 company faced challenges in meeting its local tax compliance needs with fewer in-country finance professionals.

Instead of continuing its country-by-country approach to sourcing, the company switched to a regional strategy and sourced all of its compliance support, including corporate income tax, indirect tax, and local and US GAAP tax accounting, from one tax service provider.

Doing so freed up time for the company's in-house tax teams to provide business-critical support. Through their provider, the teams now had access not only to leading compliance and risk management practices but also to the provider's own investment in compliance technologies. The teams also gained informed tax advice on developing tax legislation, business issues, and acquisition and divestment transactions on a consistent basis across all territories.

A key motivation for outsourcing was tax savings, and the provider pursued opportunities in all markets. Within 6 months, local and regional brainstorming sessions identified opportunities in three countries, and a review of prior-year returns accelerated over USD5 million in cash tax refunds.

Blueprint for change

Respondents report a surprisingly high degree of satisfaction with levels of investment in tax department processes and technology. The majority of them also report that their tax controls, policies and procedures are standardized or very standardized. Nevertheless, a sizeable minority of respondents are less progressed, and fewer than 40 percent say they are "integrally involved" with wider finance function transformation initiatives.

The case studies in this section show that taking a proactive approach to reviewing and improving the efficiency and effectiveness of tax processes can produce considerable benefits. Even more gains can stem from engaging with the wider finance function to ensure the accounting processes that tax departments rely on succeed in supporting their needs. Our experience is that tax departments can do much more to improve efficiencies across their core activities. We recommend that tax department strategies should address opportunities to:

- refine and embed efficient processes that realize the strategy in ways that are monitored and sustainable over the long term;
- establish systems and procedures to produce, exchange and distribute timely, accurate and relevant information to the right people at the right time and in the right format; and
- employ enabling technologies to automate labor-intensive and manual processes that consume resources and increase risk.

> "I think the service providers do a great job, if you choose the right one. You have to have really a good selection process. Making the right choice opens up a lot of time that you can then dedicate to issues like tax disputes and planning."
>
> **— International tax and reporting director of a leading extractive industries company**

Improving connectivity – more work to do?

Tax directors of leading tax departments take proactive steps to develop a strong understanding of the tax and business environment within which they operate and to engender close integration with the business colleagues they support. Helping the company make the most tax-effective decisions in line with its broader business objectives and proactively bringing ideas to help achieve those objectives are hallmarks of a well-integrated tax department.

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By moving beyond tax compliance and working closely with all parts of the business, tax departments can help their companies avoid missteps, identify opportunities and add greater value. The key is timely awareness of potential events with tax implications. Tax resources can reach out to business units to provide tax briefings to key decision-makers, alerting them to the types of events or transactions that may have tax implications. In turn, business units can include tax in strategic and tactical planning sessions.

While the survey reveals that vertical alignment between tax leadership and the board is being achieved, less priority is given to increasing horizontal alignment with other business functions.

When asked where their tax department will devote its time over the next 12 months, tax compliance and financial reporting are the highest ranking. These activities are expected to occupy 20 percent and 19 percent of tax department time respectively. Combined with the amount of time spent managing tax audits (11 percent), these compliance-related activities occupy just over half of tax departments' time. Other, more forward-looking, higher-value activities — such as optimizing the effective tax rate, cash tax planning, tax process improvement and integration with business groups — are expected to take up only about one-third of the tax department's time.

As noted earlier, the focus toward compliance activities is also reflected in the importance put on various tax department responsibilities and on the KPIs to assess performance. As also noted earlier, for tax departments that will restructure in the near future, better alignment with the business or finance function is the least common reason for change. Reducing costs and improving controls, efficiencies and risk management are cited more often.

55% of respondents have employees with tax responsibilities for business units or divisions

50% of employees with business unit responsibilities report to the headquarters tax department

The trend toward centralization can also hamper tax departments' ability to focus on better connectivity with all parts of the company. When tax teams assemble in central locations, they typically have less opportunity to engage with teams in other countries. This can contribute to a perception that they focus solely on tax compliance versus supporting and understanding the broader company. This type of situation is even more challenging when other finance and accounting functions are also centralized.

Companies that adopt centralized tax department structures need to put in place measures and procedures to ensure tax teams have the opportunity to contribute and can be a part of decisions and activities where tax has an impact and can increase or decrease value.

A possible opportunity being employed by 55 percent of respondents currently, is having employees dedicated to particular business units or divisions. However, while these employees are presumably better connected with the business segments they support, the benefits of centralization may be forgone: only

Approximately what percentage of your tax department's time will be spent on each of the following activities over the next 12 months? (mean %)

Accurate/timely financial reporting	20%
Accurate/timely tax return compliance	19%
Optimizing the effective tax rate	11%
Management of tax authority audits	11%
Cash tax savings/tax deferral	10%
Managing tax risk	8%
Tax process improvement and technology utilization	8%
Integration with business groups and early indication of non-routine transactions	7%
Influencing tax policy	6%

Source: KPMG International 2012

half of respondents say that these employees report directly to the headquarters tax department while the other half report to regional finance, accounting or tax personnel.

Developing and embedding processes to facilitate better integration and collaboration takes time and resources. For some tax departments, this may require a thorough review of current structures and priorities. The challenge remains how to free resources and time to focus on a more strategic agenda that proactively supports the wider business strategy.

76%
of tax departments have KPIs for tax return compliance

Only 49%
have KPIs for integration with business groups and early indication of non-routine transactions

Blueprint for change

The survey results suggest that tax departments may need to do more to engage directly with a broader range of stakeholders in their businesses to support tax effectiveness of business developments as they happen.

We recommend that tax directors take steps to increase their influence and their tax department's perceived value by:

- developing a strategy to understand the goals and constraints of key internal stakeholders and communicating how tax can help meet objectives;
- ensuring that the tax strategy and operating structure specifies how tax department resources will be deployed to promote connectivity and collaboration among tax teams and other business functions; and
- setting KPIs to measure the contribution to the success of other business functions and to the overall bottom line.

"We have appropriate protocols in place within our organization. For example, to make a business decision, you need a tax report prepared by our department or in coordination with another tax firm. So we ensure that we are involved in all decision-making in one way or another."

— International tax director of a European-based infrastructure company

"We actually have 14 major businesses within [our global group], many of which are Fortune 500 companies themselves, and so we connect at very different levels, and not just with their presidents and CFOs. Because they're global businesses and because many of them are located outside the US, I need to make sure my team is connecting at lots of different levels. I think that's most effective because not all of the decision-making, strategy development — and of course implementation — is done at the top."

— Vice president of tax of a US-based Fortune 500 company

Meeting the challenges ahead - are tax departments ready?

The current survey results show that tax departments are doing well in improving accountability and standardization, and they seem fairly well equipped to meet the compliance obligations that are a top priority. Respondents generally are satisfied with levels of tax resources — whether in terms of administrative budgets, staffing or investments in new technology.

But what does the future hold in terms of the continuing burdens on the tax department and how might that change the attitudes of respondents?

Managing heightened levels of tax controversy

As noted, respondents expect that their tax department will spend about 11 percent of its time managing tax authority audits in the next 12 months. However, respondents report that the levels of tax controversy have increased sharply since 2009 in nearly all taxation areas. Only 38 percent of respondents are not involved in any tax controversy activity. About one-third are involved in controversy over corporate income taxes. Over 52 percent are involved in indirect tax and customs duties disputes; and when results are combined this is up from 43 percent in 2009. The number of companies involved in controversy related to transfer pricing shows a similar rise, climbing from 18 percent in 2009 to 26 percent.

In the future, regulatory changes, such as the US Dodd-Frank Act and the EU Transparency Directive, will add even more pressure on companies' abilities to meet their tax compliance and financial reporting needs.

In which of the following areas, if any, do you have controversy activity with tax authorities?

	2009	2012
Country-based (federal) corporate income tax	33%	34%
Indirect tax (sales/use or VAT)	31%	33%
Transfer pricing	18%	26%
Local (state) income tax	26%	24%
Cutoms/duties	12%	19%
People taxes (social security, personal income taxes, benefit plans, etc.)	17%	19%
None of the above (2012 survey only)	N/A	38%

Source: KPMG International 2009, 2012

Respondents also report that tax authorities are taking more interest in how well tax department processes are managed. When asked which areas tax authorities have been taking more interest in the past year, tax processes and controls are named as frequently as indirect taxes. Respondents say closer scrutiny of accounting processes and controls, tax strategy and risk management and technology are also more common.

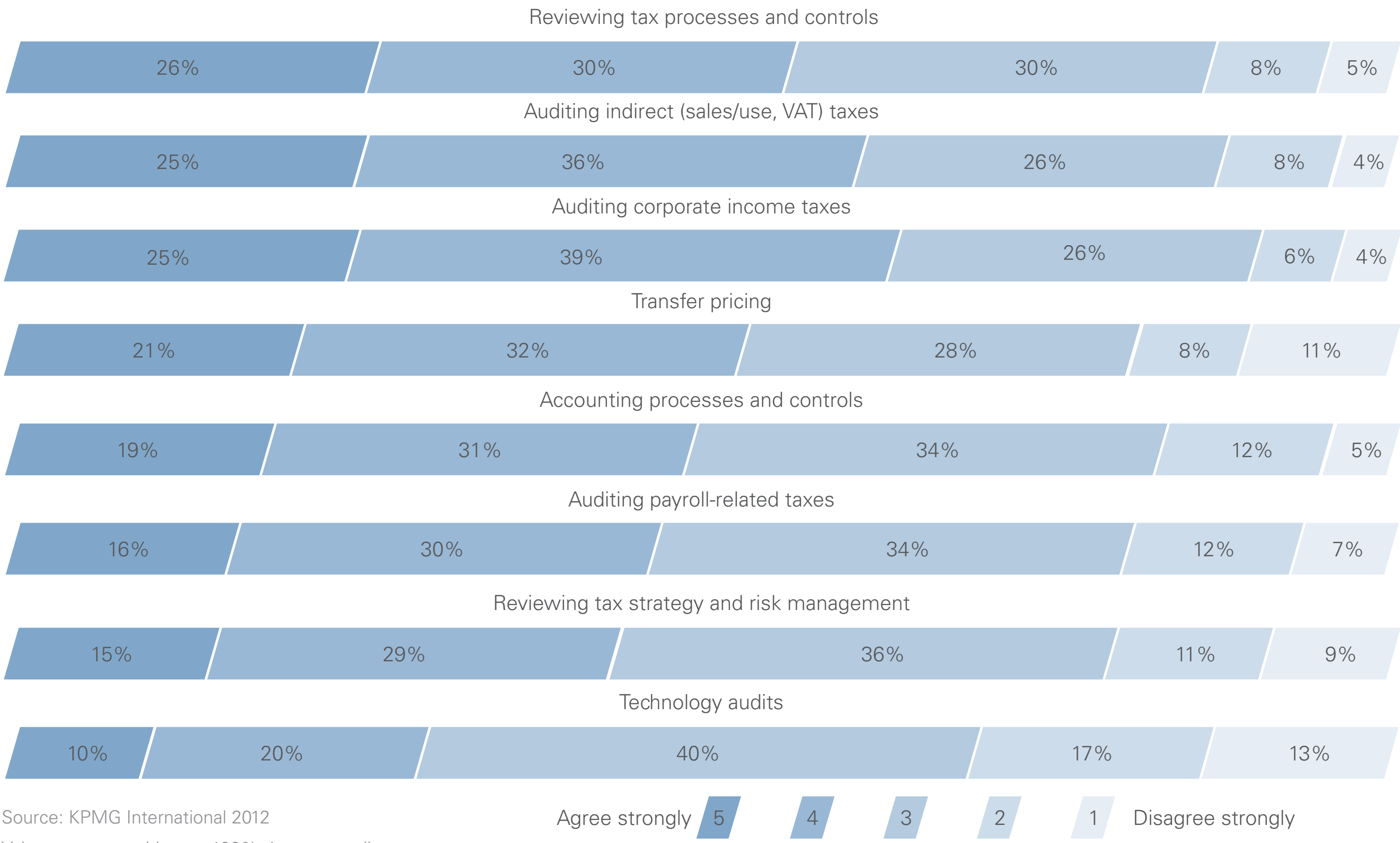
These results reflect the developing trend in tax authority approaches to taxpayer compliance. Indeed, many tax authorities are becoming more focused on assessing the ability of companies' accounting and tax processes and systems to enable them to accurately comply with their compliance obligations rather than the traditional post-filing review of the tax return to identify errors or incorrect disclosures. The priority on routine compliance and minimizing tax risk are well placed when considered in light of the increasing levels of tax audits and disputes.

Notwithstanding the importance of getting compliance right, the value of effective tax rate management, cash tax planning and business support remains important.

The challenge therefore is how the tax department can manage the increasing compliance burden while addressing the demand for value-added input. In this context, it is interesting that respondents are generally satisfied with current levels of tax department resources and investments: administrative budgets are the same over the past year for 68 percent of respondents and 79 percent say budgets are sufficient. And as noted, 74 percent of respondents say the level of investment in technology and process improvement for their tax department is "about right."

The satisfaction suggests that they may not fully appreciate what the future challenges could include — in particular, tax investigations and disputes and the developing tax authority approach to taxpayer compliance will test their ability to manage compliance in the coming years.

Over the past 12 months tax authorities are becoming more focused on:



Source: KPMG International 2012

Values may not add up to 100% due to rounding.

"I find that compliance, reporting, litigation, dealing with tax authorities have become much more difficult. It takes up a lot of our time."

— International tax and reporting director for a global mining company

Fit for the future – KPMG's blueprint for change

As tax authority scrutiny and disputes continue to rise, how can tax departments meet demands for greater accountability and transparency, adapt and add value to rapidly developing business needs, while increasing efficiency and managing cost and resource constraints?

As they struggle to cope, leading companies know that a transformational approach can show the way. KPMG's research notes the following steps as crucial elements in a blueprint for change.

Strategy – align with the business vision and strategy

As a first step, understand the broader business strategy and what the business will look like under that strategy: where will the business be in the mid to long term and how will the tax department support that vision? It is crucial for the tax department to engage both vertically with boards, CEOs and finance executives and horizontally with the business functions it supports.

Next, review the tax strategy's alignment with the overall business strategy to identify differences and barriers. Aligning the tax strategy allows the tax department to set the right goals, communicate them to key stakeholders, and establish the resources to achieve them.

Communication and measurement — set KPIs that measure all contributions

The tax department must consider how to measure, monitor and report on performance to multiple internal and external stakeholders. A key step is to set KPIs, benchmarks and scorecards that go beyond timely compliance and measure the wider contribution to the company.

Effectiveness and efficiency – align the operating model

Within the constraints of limited resources and budget, the tax department should have an operating model to best deliver on the business strategy.

By transforming how it operates, a tax department can free itself to focus on activities that add value and potentially reduce time in tax authority audits. The evaluation of a tax department's efficiency and effectiveness is increasingly important to not only internal stakeholders but also external ones.

Many tax authorities are working with taxpayers to examine how the company's finance and accounting processes enable effective tax governance and risk management. Establishing an effective, well-governed operating model will give tax authorities confidence in the company's handling of its tax affairs.

Building the case for change

In conclusion, this year's survey shows that tax departments are making great strides forward in several key areas. They are engaging their boards and senior executives to set their strategy. They are putting top priority on getting tax compliance right, and they are making progress on centralizing and standardizing their systems and activities.

But with tax compliance and reporting activities demanding more attention and time, tax departments appear to have less time to collaborate with the broader business on value-adding activities.

The challenges are immense, but we believe the current business and regulatory environment offers tax directors a tremendous opportunity to transform their tax departments and interact with the broader business and external authorities. By taking a proactive approach and building a strong case for an effective tax framework, companies can gain confidence that their tax affairs are well managed and support the overall business goals.

"I really believe that tax can make and improve our competitive advantage in transactions in dealing with both customers and suppliers. It can sweeten the whole supply chain process. If we can get tax to work — where the value is not just on the tax line — then we've added a lot more to the organization and shown our true value."
— Group taxation director of a global UK-based industrial construction firm

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.

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