Leading the Tax Function of the Future

CFO's Guide to Automation and Digital Transformation of Tax

Avalara

Tax compliance done right

Tax administration across the globe has become digitized in recent years and can be seen gaining momentum even in developing countries like India. While traditional spreadsheets and manual workflows were once commonly used for tax functions, they are now being replaced with web-based platforms that oversee most, if not all, tasks associated with indirect tax compliance. And even though organizations in India are adapting to the process of digitizing this significant part of business operations, there are several companies still playing catchup while making this transition.

At the time of writing, countries around the world are facing a pandemic, and many of them are under lockdown. Due to the new set of restrictions, companies, big or small, seem to be struggling with their tax management function. It is common knowledge that tax as a function has always been the underdog in a company's digital transformation strategy. We don't blame them. The tax function is not one that generates any revenue. This is probably why it has always been overlooked while chalking out a digital transformation exercise.

But with rapidly changing policies and the impact generated by COVID-19 on world economies, companies realize why they cannot ignore tax management and why it is important to stay on top of technological developments that can help manage their taxes better.

Most Governments are doing their best to provide tax relief and have provided their taxpayers with several measures like extensions in tax deadlines, accelerated refunds for better liquidity, even exemptions. But even after all of these relief measures, organizations who haven't digitized their tax function yet are likely to hit the ground running before or post lockdown.

Before answering how to digitize a company's tax function, due diligence must be given to understanding what digitization of tax does for companies, why is it necessary and the most significant question - which person must carry out the role of digitizing the tax function in a company.

The whitepaper outlines the impact of digitizing tax compliance early in the process of implementing a DX strategy, the role of the Chief Financial Officer (CFO) in helping a company adopt new technologies and processes, and the strategy and skills required of businesses to successfully crossover into the digital age.

Haven't thought about digitization of tax yet?

Here's some food for thought

Ordo ab chao is a Latin phrase which means order in the chaos.

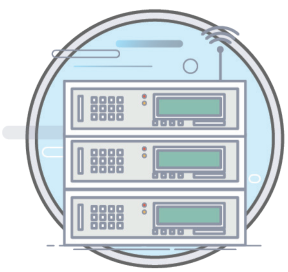
A traditional tax system is renowned for being wildly chaotic. Riddled with errors and loopholes, it can have the taxpayer running from pillar to post irrespective of deadlines. Such a system is not only difficult to enforce, it gives way for tax evasion and tax fraud - two phenomena that ultimately lead to higher taxes each year. The result - taxpayers are frustrated out of their minds, working twice as hard but not really being very productive and still end up paying more out of their pockets. Adding fuel to this fire is the additional cost of time and wasted energy that could have been better optimized.

Needless to say, organizations still using traditional means to address their tax functions are wading knee-deep in manual and error-prone processes, leaving little or no time for improvement. How do we bring about a sense of order in this chaos?

For a company that has not made the transition from traditional paper-based tax functions or digitized tax functions to a fully automated one just yet, it is important to break down the tax function by its existing problems areas. When we breakdown the function by problem points, we can fully understand the depth of issues that can be addressed when a company finally starts transforming its tax function.

Transparency

Tax is not just a function; it has a lot more riding on it. To quote an article by PWC Global, 'tax has become a reputational issue.' A number of stakeholders, internal and external, demand to know about the tax function of an organization. These stakeholders include the government, media, customers, shareholders, and even the employees of the organization. Digital transformation helps maintain transparency in all functions of the organization, including tax. The fact that transparency can be maintained in a department which is otherwise kept away from the limelight means that it now opens avenues for becoming a part of the organization's external communication message.



Efficient data management

Because there is an exhaustive amount of numbers, it is urgent and highly necessary to manage this data efficiently and effectively. When you introduce technology solutions into this function, the data is not just sitting around. The tax function will be able to make use of technology that will manage information to meet regulatory requirements and make better and informed strategic decisions. An added advantage of well-managed data is that organizations can plan well in advance for better tax planning, scenario forecasting, and predictive analysis.

Better compliance

In a 2018 study by IDG (International Data Group) on the future of business, it was found that of the 89% of organizations that planned to adopt a digital-first business strategy, only 44% have fully implemented the approach. Additionally, developing nations lose nearly $1 trillion per year due to illicit financial flows. While it is common knowledge that the public sector is bound by regulations, a lack of digital skills, and a lack of awareness around the benefits of technology-based solutions, the same cannot be said for the private sector. With more awareness and a keen interest in actively making a transition, private organizations are steadily altering their budgets to incorporate technology-driven solutions that will help better their tax compliance.

Security

In India, the security of sensitive data, especially tax-related data, is a major concern for enterprises considering a digital transition. In retrospect, traditional security solutions cannot guarantee data security. On-premises security is only as reliable as the security policies enforced at an organization. By making an effort to automate the tax function, organizations will be required to employ the services of cloud-based service providers, who are known to provide the highest data security standards.

Eliminating manual processes

A majority of the time and energy spent by compliance teams is on manual processes. But when you have technology looking after mundane tasks like tax reporting and invoice generation, you have the time and the resources to shift focus on business transformation. This enables your risk and compliance function to actually add value to your organization rather than tick off a list of business-as-usual activities.

Keeping up with dynamic regulations

In a developing nation like India, which is still fairly new to tax reforms like the Goods and Services Tax (GST), organizations have had a harrowing time keeping up with changing regulations. One of the advantages of digitizing an organization's tax function will be the department's newfound ability to keep up with changing regulations, thereby reducing the scope for error.

Value addition

By incorporating a digital transformation exercise, your tax function will be able to identify risk faster, create data-driven recommendations, and help reduce costs, while simultaneously partnering with other areas of the business. Thus, companies will be able to create and drive value by leveraging technology and thereby improving your organization's efficiency.

Why the tax function?

A digitized tax function is a part of a paradigm shift brought on by rapid globalization, growing regulatory and business complexities and continually evolving tax technology. And even though the tax function is slower in adapting to a digital transformation exercise, the tax function needs to be a part of the practice. For a digital transformation strategy to work in any organization, the departments of finance and information technology need to be working in tandem. Considering that the finance department does not work in isolation, and its functioning impacts all corresponding departments, more organizations are introducing their finance, risk, and compliance teams to digitized solutions. But why digitize the tax function?

Across the globe, tax authorities are setting sights on technological developments and solutions to enable digital tax collection as well as analysis of tax information and data. Real-time reporting, standardized audit files and invoicing formats, use of artificial intelligence to reduce manual entry of data are just some of the strides taken up by tax authorities across the world.

Governments world over are displaying a willingness to adapt digitized solutions to better their tax collection systems. In such a time, it becomes imperative and urgent for taxpayers to align themselves with digital processes followed by authorities. That way, they don't play catch up all the time.

ABCs Of A Successful Digital Transition of Tax Function

Success is a highly perceptive concept, so when we look at successful digital transformation stories, each business will have a different way of measuring how well they have transitioned. Nevertheless, a clear pattern seems to emerge from almost every successful case study, and we can see that a digital transformation exercise is driven by three critical factors.

- **Adapting to technology**
- **Creating a seamless experience**
- **Onboarding digitally savvy leaders**

While there are several factors that drive a digital transformation exercise, these three factors are pertinent to a CFO looking to take up a DX exercise. Think of these critical changes as a blueprint.

A. Technology

Technology makes up a significant part of any DX strategy as the solutions adopted by a company will drive their operations. Most companies undertaking the exercise of digital transformation are likely to select one or preferably more technological solutions that will help automate manual tasks, help analyze data, or even improve store and secure data. While there are several types of technical solutions, we have bottled down a few that are ideally suited while digitizing tax.

Automation technology

Robotic Process Automation or RPA software is a type of software that can imitate any kind of physical activity tasks that do not require knowledge or human understanding. They are primarily designed to interpret manual, mundane tasks that are repetitive in nature and include data validation, data entry, data reconciliation, etc., thereby freeing up human resources for tasks of higher value.

Analytical technology

With tax authorities introducing advanced technology to collect, store, and analyze tax and financial data (e-invoicing[1] and GST new returns[2]), it is only a matter of time until organizations will need to shift their mindset and jump on the bandwagon and incorporate tax data analytical tools. These tools can convert data to information and, ultimately, insights for key decision-makers, sometimes even in real-time.

Cognitive technology

Machine learning and AI-driven computer systems are now advanced enough to be incorporated into an organization's corporate tax function. These tools are capable of performing tasks that traditionally required human intervention but can now be automated. Such duties include forecasting, ensuring processes, and meeting regulatory requirements.

Data wrangling technology

Data wrangling tools that have been explicitly designed for tax can help the tax function in an organization work their way through mountains of data. Data wrangling tools are designed to retrieve raw data, including semi-structured and unstructured data, and process that data, making it available for easy and efficient reporting.

Cloud computing technology

An article in Forbes suggested that cloud technology will take precedence over on-premises technology in the near future, with more than 80% of workloads moving to cloud by 2020. In the tax function, cloud-based applications can help standardize the tax processes of an organization across the country or even globally. These applications can also reduce the need for IT to maintain systems, enabling those professionals to focus on higher-level strategy.

[1] E-invoicing in India: E-invoicing was officially rolled out by the Government of India in January 2020 and this new system promises to change the way organisations deal with the country's largest tax reform, the Goods and Services Tax. One of the major issues faced in the current version of the GST returns filing system is that information is uploaded manually across varied invoice formats – obviously leaving a large scope for human error. Subsequently, taxpayer returns have been riddled with mistakes resulting in mismatched data and a large gap in data reconciliation. Hopefully, with a standardised invoicing template and the fact that this template can be read by any accounting software, invoices are now interoperable between software. Fewer errors will lead to faster availability of input tax credit, lower probability of tax audits, an efficient collection system and a possible containment of tax evasion.

[2] GST new returns: In its 31st GST council at the end of 2018, India announced the implementation of a New GST Returns system. This system is likely to be implemented in April 2020 and will contain simplified return forms for ease of filing across all taxpayers registered under GST. Currently in its trial phase, this New GST Returns System will be introduced in a phased manner with a view to familiarise users with the annexure forms of the system.

B. Seamless experience

For a successful transition, organizations cannot focus on digitally shifting a single department. Their digital transformation (DX) strategy will need to encompass everything from manufacturing to after-sales services. Although the process will take some time, organizations that have successfully undergone digital transformation have had to play by the 'all or nothing' rule. A primary agenda behind a DX exercise is to help create a seamless experience. Under the tax function of an organization, digital transformation involves the seamless integration of tax governance, data management, and collaboration.

Tax governance

Tax governance is the first step in building a seamless experience for an organization's tax function. It includes the capture and storage of data. While companies have traditionally used paperwork or rudimentary technology like spreadsheets to gather data, they will use Enterprise Resource Planning (ERP) solutions as a part of their digital transformation exercise. This data will be collected from various departments and will be collated and stored at a single source. Traditionally, companies relied on on-premises storage solutions, but under digital transformation, the company will move to cloud-based storage.

Data management

Sorting through and understanding mountains of data has always been a tough task, but such a job gets nipped in the bud when an organization undergoes digital transformation. Once the tax data is stored on a cloud-based storage solution, it can be accessed in real time by tax data analytical software. This analytical software can help organizations gain insights and thereby design better strategies in the future.

Collaboration

With real-time access to data that hasn't been left to stew, organizations can work on creating an end-to-end tax life cycle process by visualizing their tax data and its resulting predictive insights.

C. Digitally savvy leaders

There is more to a digital transition than merely adopting new technology. Organizations might migrate from an on-premises system to a hybrid cloud or software as a Service (SaaS) technology, or they could employ ERP solutions. They could even enhance the customer experience as a part of their digital transformation exercise or create a multi-channel experience. Still, without adjustments like having digitally savvy leaders in place who have the vision to build capabilities, one can hardly say their digital transition is complete. This next section of the whitepaper focuses on the role of the CFO in digital transformation.

Digital transformation and the CFO

Digital transformation is as financially driven as it is technology driven. The IDC, or International Data Corporation, has predicted that between 2018 and 2021, companies around the globe are likely to spend over $6 trillion (collectively) as a part of their digital transformation exercise. Chief Financial Officers around the world will be or have already been bombarded with internal funding requests, and this is why they play a vital role in any organization’s digital transformation exercise.

Why CFOs must drive digital transformation

Considering the critical responsibilities of a CFO are financial planning and capital allocation, their role is crucial to the successful digital transformation of an organization. A CFO has the vantage point on critical data flow in an organization that is not limited to finance. This data runs deep in sales, supply chain, operations, marketing, communications, and business performance. Knowledge of such data allows the CFO to prioritize transformation exercises and oversee change management in each department.

At the time of writing, the novel Coronavirus pandemic has put DX goals into perspective for organizations. In the last quarter, as companies struggle with the lockdown, more CFOs are recommending that companies direct their investments toward automation systems as operations are gradually being altered to accommodate remote working. In such a time, organizations can get firsthand experience of how automation systems are suitable not just for the finance team but also for different operations.

Role of the CFO in digital transformation

Any seasoned CFO worth their salt and those who have actively led their organizations into a digital transition will tell you that one of the first activities they take up under digital transformation is to bring about changes on home turf. If a tax digitizing blueprint were to be followed, a CFO would, for starters, conduct a thorough assessment of their current tax processes, existing automation, analytical capabilities. Based on their assessment, a CFO will be able to chalk out a robust plan for a new model.

This new model would drive changes in the Finance, Risk, Compliance, and Tax departments. That being said, this will only be the first leg of responsibilities a CFO will undertake. As a driver of digital transformation, a CFO will be required to take up and see through several challenges.

Cultivate change

The world has witnessed top-ranking organizations being knocked off their pedestals because they underestimated the rapid rate at which consumer behavior, demand, innovation, and competition changed. While it is the CEO’s job to drive business, it is the CFO’s job to drive the financial systems and processes to achieve holistic growth. With changing times, the most significant change today is digital transformation. Unfortunately, case studies of many failed DX strategies have shown that finance departments make this transformation at a painfully slow pace which eventually makes the tax function a cog in the wheel. Tax functions that are open to exploring digital technologies will find themselves on the path to the 'function of the future' and will discover the strategic role they play in an organizations' success. Keeping this vision in mind, CFOs need to out with the old and bring in the new.

Make the most of data

One of the most important lessons we can learn from data science is knowing what we have. Even though mountains of data are mined every single day, companies need to take a closer look to find out what they already have at hand. It is upon the CFO to drive insights from this data and use those insights to forecast the next moves of the organization. Imagine the scale and degree of accuracy of decisions CFOs could make and at a rather quick pace too if they had data that would help them see right. This could potentially eliminate the reliability of past performance as the foundation for future decisions.

Business model evaluation

CFOs play a significant role in determining which digital business models may be economically viable for their firms, depending on the short-term and long-term objectives of the organization. Such digital business models help them prioritize which function of the company needs to have their requests approved first, how much it will cost the organization, and how much time it will take the organization to start to see returns.

Measuring digital transformation

A digital maturity index intends to measure how far a company has progressed in its use of modern digital facilities. It illustrates a growth chart that tracks an organization's progress by rising from the static stage where a business could lag to the progressive scene under which an organization has actively taken steps toward digital transformation. Indian news publication, the Financial Express, recently published an illustrated progress chart to understand a digital maturity index (Exhibit A) better.

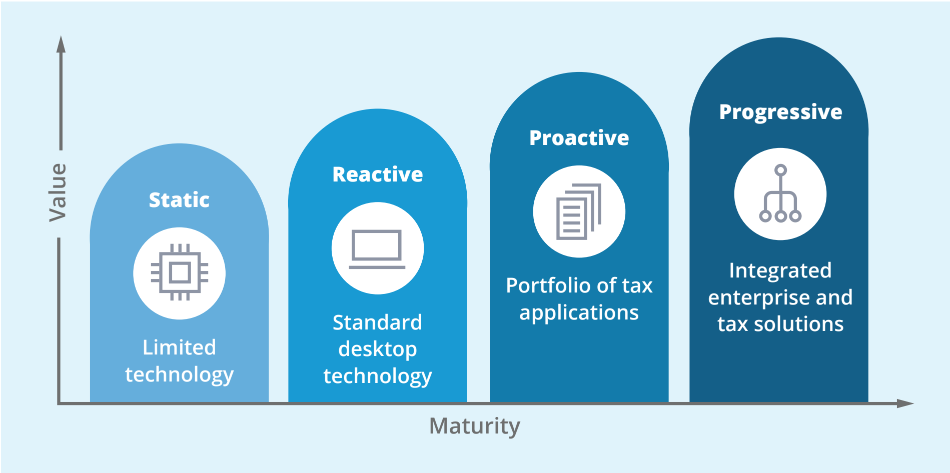


Exhibit A

At the reactive level, tax functions can speed up current analysis by ensuring that data is accessed from a single location. They can also put databases in place to support the spreadsheet analysis performed through the tax function, using standard desktop technology – fundamentally, it is a step up from traditional paperwork.

The next step is when an organization proactively seeks a defined data management process. These include actively working on data visualizations of analytics, connecting tax systems from different processes or vendors, and leveraging key data points from various systems to provide data validations. The objective at this stage is to create a portfolio of tax applications.

At the progressive stage, the tax department will undertake advanced tax functions that will define data patterns, improve data quality, implement data wrangling tools to streamline data between different systems and begin adopting predictive analytics for tax planning.

At the highest level of maturity, leading organizations will embrace cognitive computing and machine learning to reduce or autocorrect irregularities across transactional data and start implementing natural language processing, data mining, and text analytics to work with unstructured data.

Where do Indian organizations rank on the Digital Maturity Index?

A digital maturity index could be used to measure the maturity levels of departments under an organization, including the tax function. According to an Ernst and Young TaxTech India Survey, about 45% of Indian companies use basic infrastructure for tax accounting, 24% of Indian companies use tax software with no integration with ERP systems, and over 90% of the organizations admitted that their tax compliance systems are not automated. With such startling numbers, Indian organizations urgently need to work on their digital maturity index ranking.

Organizations in India can choose from the following options for turning these statistics around:

- Prioritize tax function technologies and develop the skill set of the in-house staff. Although this task needs a considerable amount of investment, it will help organizations get on the path toward a digital transition.
- Outsource the tax function partially and collaborate between in-house personnel and third-party service providers.
- Outsource the tax function to a tax technology expert and have a third party ensure that tasks, including tax reporting and filing, are undertaken accurately. This option is by far most cost-effective and allows the organization to excel in its tax function discipline.

Digitally transforming tax administration in India

In a recent interview, the CEO of the Goods and Services Tax Network and the Commissioner of the Income Tax Department of India indicated that compliance with tax regulations consumes a considerable amount of businesses' time as well as energy. Hence the urgent need to increase reliance on technology. Additionally, with the Central Board for Indirect Tax and Customs (CBIC) rolling out the new GST returns system that can be updated in real time, the use of technology is becoming critical for tax management in India.

India is also helping its taxpayers become cognizant of the need to take up digital transformation initiatives. A government-led initiative called Project Insight was rolled out by the Income Tax Department with the agenda of promoting compliance, imparting confidence, and facilitating fair tax administration. An essential aspect of this project was the Compliance Management Centralized Processing Centre, which campaigns for compliance and encourages taxpayers to make use of the tax reporting portal.

Subsequently, numerous digital initiatives for compliance have been carried out by the indirect tax department as well. For instance, Manthan, a GST Awareness Campaign, was one of the most significant initiatives of the Central Board for Indirect Taxes and Customs. Under this initiative, workshops on GST compliance are being conducted in different regions of India since 2017. The Goods and Services Tax Network will also be providing accounting and billing software options to small taxpayers transitioning into the e-invoice system for free.

That being said, one must consider the volume of taxpayers in India before determining the reach and success of government-led awareness initiatives. There have been several region-specific studies that have concluded that businesses do not have a complete awareness of GST norms and thereby might not have sufficient information to take steps toward digitizing their processes. Without adequate know-how, it would be unrealistic to expect businesses to update their software or adopt digital tax solutions.

Beyond COVID-19 for Indian Businesses

The Goods and Services Tax was introduced in India in 2017, and in the last two years, the government has stressed the need to defect from traditional tax functions and incorporate tax technology. While the government can only go so far with free software solutions, help desks, awareness initiatives, it is the primary responsibility of the organization to recognize the urgent need for digital transformation and take the necessary steps toward making a transition. These steps include setting up critical goals for the organization by focusing on areas that need changes effective immediately. Organizations could also do better with a holistic tax plan that can encourage transition without halting any functions that might already be in progress. Not every organization will see value in being abreast with technology solutions. But one must bear in mind that organizations can conduct a cost-benefit analysis to determine where they want to be in terms of successfully transitioning to a technology-driven workplace. It is when organizations narrow down factors that will help with a successful transition exercise and actively work toward achieving this goal that they stand to land a spot on the progressive end of the Digital Maturity Index.

Scratching the surface!

As we enter the second half of 2020, we're bound to see many more tax changes take effect around the world. With Avalara tax compliance solutions, you can focus on your business, and you can simply automate tax function – and let us worry about the changes.

Avalara can help to automate your tax compliance

We offer a full suite of solutions and services including resources that help to identify your obligations and registration services to ensure compliance when you expand in India or internationally.

Our cloud-based technology integrates with hundreds of ERP, accounting, billing, PoS and e-commerce platforms to bring tax automation into your expanding business, both in terms of calculating accurate taxes as well as filing returns.

To find out more about successfully managing tax compliance and growing your business in India and around the world, get in touch today.

To learn more,
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