Is your tax function optimized?

Getting tax optimization right can take different forms

Executives are challenged every day to drive optimal performance in each functional area of the organization, including tax. Given the current tech and information age as well as constant changes in tax and other regulations, an executive needs a tax operating model that drives performance and works best for the specific business. The question you must answer is: What approach is right for me?

Many executives want a simple solution; however, in today’s environment there is no one-size-fits-all approach to managing a tax function. For starters, different companies vary in their requirements and needs depending on how they are structured. Public companies, private companies and even private-equity-owned companies all differ but that is not all. Factors vary way beyond entity structure. The key is to understand those factors and plot out your journey to find the best approach for you.

Consider your current state
To understand where you want to go, start with a detailed understanding of where you are right now, by answering questions such as the following:

1. What areas of tax does the tax function currently manage?
2. What value does the tax function provide?
3. What is the fully loaded cost of your tax function?
4. How does your tax function meet and stay current with all regulatory and legislative requirements and continuously monitor the changing landscape?

8 executive pain points

1. Reducing costs while promoting efficiency
2. Reducing effective tax rate and increasing earnings per share
   Identifying permanent tax-savings
3. Retaining employees
   Dealing with planned headcount reductions or other headcount dilemmas
4. Managing tax- and finance-related risk
   Decreasing inherent risk within both functions
5. Re-evaluating tax and finance decisions given enhanced stakeholder scrutiny and reputational risk
   Accommodating decreasing tax- and/or finance-related decision support
6. Dealing with constantly changing global tax information reporting requirements
   Keeping up with change while maintaining transparency with financial and taxing authorities
7. Dealing with frequent organization changes due to high number of acquisitions
   Having processes in place for acquisitions and growth
8. Staying on top of tax data analytics
   Creating more powerful tax planning and forecasting capabilities.
Define your future state: ‘Dream up the possible’

Defining where you want your tax function to be will help identify the gaps in your current state. No two companies define their tax goals the same way. Resist the urge to follow a trend and instead pave your own thoughtful, pragmatic path to a tax operating model that works in an optimal way for your needs. For example, resist the temptation to be enamored with a specific technology just because “everyone else” is using it. Instead, evaluate what makes sense for you. Determine what your requirements and “love to haves” are, then determine what technology best meets those needs.

Questions to ask in that regard are simply a variation of the ones you used to define your current state. Truly innovative leaders answer key questions without considering limitations. They “dream up the possible.” Start with some basics.

1. What areas of tax DO you want your tax function to manage?
2. What value DO you want it to provide (such as maximizing R&D tax credits or an overall reduction in the effective tax rate)?
3. How DO you want to meet your regulatory and legislative requirements?
4. What best practices should you consider? Etc., etc.

Coming to terms with traditional approaches

**Tax insourcing** is performing a business function internally, either independently or with the help of a third-party provider that works onsite. The goal is to build an internal tax function that manages all the tax-related affairs of the company.

**Tax outsourcing** involves contracting out a business process or function to another party. It sometimes involves transferring employees and assets from a company to a third-party provider — a “lift and shift” as it were — but not always. Basically, it means hiring a third-party to manage all tax-related affairs of the company.

**Tax co-sourcing** involves partial outsourcing, whereby a business function or process is performed by both internal staff and an external party, such as consultants or vendors with specialized knowledge of the business function. In the context of the tax function, this means that both internal and external resources share the responsibility of managing the tax function. Some responsibilities are primarily owned by internal resources and some are primarily owned by external resources. This option has the most variation and is often considered a solution that allows the best of both worlds.
Then move into some of the more forward-thinking questions:

1. What information do you want for a real-time understanding that helps you make more informed decisions? For example, you might want to understand what type of credits and incentives are available in locations where you wish to expand.

2. How can you unearth tax savings to support strategic investments in other areas of the organization?

3. What aspects of the business strategy might have a significant impact on tax, and what alerts do you need built when it does (such as around product pricing fluctuations that affect transfer pricing policy)?

Understanding what you have and what you want or need will help define the journey you will need to take and the value-criteria you will use to make choices.

**Choose your path now and be agile**

Now for the tough part: weighing your options. With a clear vision of what you need and what you want out of your tax function, which approach best suits you? In other words, do you insource, outsource or co-source? (See the sidebar on page 2 for an explanation of terms.) Each approach has pros and cons. Let’s discuss further those three options.

Truly innovative leaders answer key questions without considering limitations. They ‘dream up the possible.’
Why insource tax?

1. To maintain control of critical production or competencies and maintain strong accountability
2. To collaborate with functions like IT, which is increasingly entwined in every aspect of the business
3. To drive innovation that directly benefits the business, not the outsource provider
4. To lower the real cost of internal resources
5. To invest in internal capability
6. To easily access talent required to support the function
7. To support a political and cultural sentiment against offshoring, which has become a major cost-competitive solution

Case study: Insourse

Outside partner gets an in-house tax function on track

A large private company outsourced its tax function in the past and sought to bring it back in-house with the arrival of a new CFO. Although the CFO hired a tax director, the tax director had no experience building a tax function from the ground up. She partnered with a third-party provider that helped her develop a blueprint of the future-state operating model. It included details around the people, processes, data and technology needs to support it. Now armed with a blueprint, she was able to start putting the right pieces together. With an effective tax operating model in place, the tax director was able to explore not only how to address the daily requirements better but also how to better leverage emerging technologies to capture meaningful insights and help the company achieve its strategic objectives. When one of the strategic objectives became an initial public offering, the company benefited from its investment in its internal tax operating model, as the tax team was able to support that effort with ease and raised the capital it needed to grow the company. Today the tax director works with a third-party provider occasionally to review revised future-state operating objectives in order to stay current with the changing landscape.
Why outsource tax?

1. To allow management to focus on core competencies to move the business forward
2. To lower the real cost of managing the tax needs
3. To avoid a situation where tax resources are hard to find or keep
4. To stay current with the changing regulatory and legislative landscape
5. To have the “right” number of resources to support the volume of tasks
6. To access world-class expertise for every functional area
7. To gain access to world-class technology and the latest innovative trends without a massive investment in technology

Case study: Outsource

Inefficiencies and a bankruptcy scare led a multinational to outsource tax

A multinational public company did most of its tax work internally through a tax department of seven individuals, each operating without a defined role or set of responsibilities. Management felt strongly that an in-house staff could do the work more cheaply and efficiently than an outside firm. Yet when the business began to slide into bankruptcy, management decided to scrutinize all areas, including the tax function.

Management uncovered several inefficiencies, including software licenses for several products that the tax department paid for but wasn’t using to full capabilities. More research led management to conclude it should outsource the tax department to a third-party provider. Management valued the provider’s understanding of the company’s challenges and its introduction of current technology and automation solutions, which the organization desperately needed. The third-party firm also offered enough tax personnel to handle each competency area, greater visualization into the company’s global tax posture — and ultimately a lot more bang for the buck.
Why co-source tax?

1. Flexibility
2. Control of key work streams
3. Access to a tax specialists on an as-needed basis
4. Diversity – the ability to work with multiple service providers depending on areas of experience required

Case study: Co-source

Co-sourcing transforms tax function into strategic partner

A services company had been performing all its own tax compliance and provision work, with occasional tax planning assistance from consultants at various firms. The approach worked in its own way, yet the company also found it was experiencing a lot of turnover in the tax area, with job dissatisfaction being the primary culprit. It also longed to be more efficient by bundling all its technology components within tax, yet lacked the resources in-house to develop, enhance and maintain such an undertaking.

Management realized that the investment needed to modernize and maintain all technical competencies internally would prove to be a significant time and financial burden. They concluded they would minimize the burden and save money by co-sourcing the tax function in a broader way, relying on a third-party provider to assist with tax planning and other daily tasks.

Initially management found comfort just in knowing its co-sourced partner could fill in the gaps when turnover occurred. Ultimately, after the co-sourced partner suggested and implemented a new technology and automation platform in a cost-effective way, management came to rely on its co-sourced partner to make the innovation leap more economically. The company’s tax professionals found themselves spending less time on tax-return preparation and more time with tax planning. Job satisfaction increased, and the tax department became more a strategic partner than a cost center.
As your business grows and matures, the search for a competitive advantage will always exist. The need to have different elements under control in-house or to outsource to specialists may change, so it is important to review your requirements regularly.

Tax function specialists may help provide solutions that help you perform at an optimal level.

**Is technology enabling you?**

At no time was it as possible as it is now to free your tax function of daily tasks in order to focus on strategic decision-making and advancement. Tax-specific technology is increasingly able to speed, notify and analyze in efficient and accurate ways. Because of its crucial strengths, tax technology is claiming greater company investment.

The question is how tech investment figures into your company operations. Many in-house tax functions don’t have the capacity, experience or budget to effectively choose and use ever-changing technology. And researching, purchasing and maintaining technology can be daunting and costly. More and more frequently, the decision is to collaborate with a provider to outsource or co-source. Tax outsourcing is a trend that is expected to grow by about 5% annually through 2021 (“The future of tax technology is now,” *International Tax Review*).

This is where the concept of “rent and use” may prevail over “buy and build.” Talent and tools can be paid for and owned. But the better investment might be in a provider dedicated to technology so that staff can remain dedicated to strategic alignment with wider company goals.

### Make your ‘possible’ happen

Begin to find the tax sourcing method right for you by assessing your current state and what could be done in a future state. What do you want to manage, and do you have the talent and technology in place for your needs? If not, are you ready for the heavy lift of building out both?

Your tax professionals are not necessarily tech experts, coders or programmers. The value of their skill sets lies in tax analysis and planning. For such priorities as tax compliance, preparatory data manipulation and processing can be a drain on time and attention.

Outsourcers provide the pertinent tools and services, ranging from performance of mundane tasks to facilitating data analytics. They can choose the right technology and automated processes for your company needs and keep those up-to-date.

It isn’t an all or nothing proposition. For your company, outsourcing entire functions might be the way to go. On the other hand, a co-sourcing arrangement could make more sense because of resource and budget allocations. A thoughtful evaluation is the key to getting your company’s tax operating model in line with your overall business objectives.
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