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Why IT managers should care about indirect taxes

White paper

IT professionals don't normally spend much time thinking about how indirect taxes are calculated or the extent to which incorrectly managed taxes can drain an IT department's resources. But it may be time to start, especially if your company's tax and finance departments are considering a technological upgrade.

That's because indirect tax management is increasingly seen as a strategic asset to the organization, not just a regulatory requirement. At the same time, the ongoing shift toward digital taxation means more scrutiny from regulators and pressure to provide more real-time tax information — all of which IT must understand and support. Failure to calculate and report indirect taxes correctly can also result in extensive audits, massive data pulls, and hefty penalties, not to mention lost time and money, tarnishing of the brand, and additional stress on IT staff.

If you've ever been involved in an indirect tax audit, or ever had to respond to multiple requests for data sets from the indirect tax department, you already know the pain corporate taxes can inflict. That pain can be especially acute when working with a patchwork of legacy IT systems and a tax department that still does some, or all, of its work manually in Microsoft® Excel.

Shifting towards digital taxation means more scrutiny from regulators and pressure to provide more real-time tax information that IT must understand and support.

Fortunately, the indirect tax burden on IT can be almost eliminated by incorporating an end-to-end tax automation solution that easily connects to the company's Enterprise Resource Planning (ERP) and other systems. Convincing finance managers to adopt such a solution can be its own challenge, of course — but IT professionals who understand why such a move makes sense are in a perfect position to help management avoid costly indirect tax errors in the future. This is especially true if your company is involved in a merger or acquisition and is migrating to a new ERP system. Deploying an indirect tax engine concurrently with an ERP upgrade or implantation ensures that all data points are available for calculating tax and avoids the need for costly change orders.

In any case, organizational growth spurts are the logical time to re-evaluate IT systems and processes to make sure the enterprise is prepared for the demands of growth. And periods of technological transition are an ideal time to introduce new software and acquaint departments with more efficient, effective ways of working.

Why should IT care about indirect tax?

IT personnel should understand the overall business implications of indirect taxes on their organization for several reasons, not the least of which is that governments around the world are relying more than ever on indirect taxes for revenue and subsequently tightening the regulatory structures governing them. This push for more indirect tax revenue coincides with a parallel desire for more transparency and accountability in all forms of taxation, as well as an across-the-board trend toward digital tax reporting and, in some cases, real-time data-sharing.

All of these developments depend upon reliable IT systems and consistently clean data, as well as software and processes tailored to fit an organization's specific business goals and tax responsibilities. A capable, well-managed tax system also enables the kind of forward-looking data analytics and scenario modeling that can transform a humble tax department into a powerful strategic asset.

What are indirect taxes?

Indirect taxes are taxes applied to the sale of goods and services, such as a sales tax, excise tax, value-added Tax (VAT), goods and services tax (GST), or gross receipts tax (GRT). These taxes are "indirect" because they are applied at every stage of the production process of a goods or services with credits allowed for tax already paid against on previously purchased inputs. The end customer ultimately pays the indirect tax where a credit is not allowed, with manufacturers, retailers, and service providers responsible for assessing and adding indirect taxes prior to purchase, and for collecting and remitting the tax revenue to the government.

For large companies, indirect taxes are challenging because they are constantly being assessed, collected, and remitted at different stages of the production process. For example, sales taxes are based on the dollar amount of goods or services purchased and added at the point of sale with an exemption of certificate presented at each stage, whereas a VAT is a tax based on the “value added” at each stage of the production process. The consumer ultimately pays for both, but they are assessed differently and require different data to calculate.

Indirect taxes are complicated by the fact that different products and services are taxed according to different rules. Municipalities, states, and countries also have different regulations and compliance procedures, as well as different penalties for non-compliance. So, for example, a national or international retailer that wants to be tax compliant must assess and collect indirect taxes on dozens or hundreds of products manufactured, distributed, and sold through thousands of transactions every day, then remit the correct tax to authorities in the state or country in which the transaction took place, in accordance with the rules and regulations of that particular locale.

Get it wrong and trouble isn't far behind. Underpayments can result in sanctions, penalties, and extra IT legwork to re-calculate taxes correctly. Overpayment can result in lost revenue. Failure to pay or file taxes in a timely manner can result in monetary fines and, in some cases, litigation.

Integrating a cloud-based indirect tax engine seamlessly to the company's ERPs allows for faster and more accurate tax determination and compliance.

How IT resources are drained

For tax professionals, managing indirect tax obligations for even a modest-sized company can be an arduous, time-consuming task. And because governments around the world are leaning on indirect taxes to generate more consistent revenue streams, and mismanaging indirect taxes can be costly, it's no surprise that corporate tax teams are devoting more resources than ever to indirect tax compliance.

But the drain on time and resources isn't confined to the tax department; all too often, the IT department gets pulled into the discussion as well. This is especially true at companies that are constantly updating their legacy IT systems with patches and fixes to accommodate the evolving needs of the enterprise. An IT department faced with the task of creating some sort of ad-hoc program to calculate indirect tax obligations can expect to do a lot of coding on the front end, and a lot of correcting on the back end, all of which eats up time and resources that could be better spent elsewhere. Such practices can also put the organization at risk for non-compliance or create situations where a company is losing money (such as through overpayment) without even knowing it.

Compliance via the cloud

Indirect tax software solves these problems by moving data management and storage to the cloud, and by automating many of the indirect tax compliance functions that are so cumbersome and error-prone when tackled manually. By integrating a cloud-based indirect tax engine seamlessly to the company's ERP, organizations can achieve faster and more accurate indirect tax determination and compliance, because all enterprise-wide transaction taxes are automated and repeatable. There is no guesswork.

Furthermore, indirect tax software allows companies to better manage their cash flow in real time, with a much more robust array of dashboards, metrics, and tools to measure tax inflows and outflows, spot trends, strategize, plan, and report, all of which improves tax department performance.

On the IT side, indirect tax software that integrates well with an enterprise's larger ERP ecosystem gives IT departments significantly more control over different data sets, and allows other departments — as an example accounting, finance, sales — to access data they might otherwise have had to request on the fly. These capabilities in turn make it much easier to align an organization's compliance functions and expand the usefulness of indirect tax data for other purposes, such as supply-chain management or other types of strategic decision-making.

During mergers or acquisitions, indirect tax software can also serve as a single point of truth around which data from another organization can be integrated and organized. Data migration from one system to another is much easier as well because many of the complications that arise from incompatible systems and programs can be bridged using specialized import and export functions.

Overall, an integrated, scalable indirect tax solution also allows a company's tax footprint to expand without heaping additional stress on the IT department or asking the organization's IT systems to do things for which they were not designed. With an integrated, scalable indirect tax solution, your tax colleagues aren't required to do busy work, and your IT personnel aren't required to be tax professionals. By removing the multi-departmental burden of fixing tax errors and updating global regulatory changes each month, you'll save significant amounts of time, money, effort, and risk each year.

Indirect tax software provides the additional benefit of a continuously updated database of regulatory policies for hundreds of countries and territories around the world.

A tech transformation

Ideally, the incorporation of indirect tax software into an organization's IT systems would also be part of a larger, enterprise-wide tech transformation aimed at future-proofing the organization's IT infrastructure against technological obsolescence. Indeed, many medium-sized to large companies now find themselves at a technological inflection point, where the bulk and cost of the hardware-intensive systems that got them this far no longer make economic sense and cannot deliver the performance and agility necessary to keep up with the accelerating demands of the digital marketplace, including — but by no means limited to — the rapid digitization of global tax governance.

The allure of a third-party, cloud-based form of indirect tax software from Thomson Reuters® is that the resulting system requires little or no maintenance, there's no downtime for upgrades, and the system scales and heals itself automatically. IT staff no longer needs to conduct cumbersome in-house upgrades on individual servers and computers. Plus, the power and capability of the software can scale according to the organization's true needs without being slowed down by budget constraints or the physical limitations of the IT staff. This in turn allows IT staff to devote more time and attention to other issues, secure in the knowledge that their cloud-based solution is fully supported and operational 24/7.

Where taxes are concerned, indirect tax software also provides the additional benefit of a continuously updated database of regulatory policies for hundreds of countries and territories around the world. Remember, governments everywhere may be tinkering with their indirect tax regimes, but it is ultimately the responsibility of companies doing business in any given region to understand and comply with the local rules — or face the consequences. Indirect tax software not only makes it possible to stay current on changing tax regulations, applicable changes are automatically programmed into the system to ensure compliance.

The advantages of indirect tax automation

In short, global tax policy is no longer static — it is a fluid, ever-shifting framework of rules and regulations that requires constant vigilance on the part of companies that wish to remain compliant. No single person can keep up with these changes, but with indirect tax software in the company's stack they don't have to — the software's support network incorporates global regulatory changes into its algorithm and the proper tax for each product sold in each jurisdiction is calculated automatically.

The more control organizations have over their data, the better equipped they will be to manage the tax requirements of an increasingly digital future.

For IT staff, this level of automation means:

- Seamless integration with ERP and other systems
- Lower overall IT costs
- Less time and resources needed to ensure compliance
- Dependable, real-time performance 24/7
- Tools that facilitate new ways of data sharing and better transparency
- Scalable, future-proof technological capabilities and adaptability
- Unification of digital tax and finance workflows
- More resilience, speed, and precision all around
- No need for extra hardware or storage
- Better security and a more reliable network
- Higher confidence that indirect taxes are being accurately calculated across the enterprise
- Cleaner, better organized, more accessible data
- Less staff time needed for data cleanup and support
- No need for additional coding

Data is destiny

Data is the common denominator in all of these tax arrangements, so it stands to reason that the more control organizations have over their data, the better equipped they will be to manage the indirect tax requirements of an increasingly digitized future.

The reality is that governments around the world are relying more than ever on indirect taxes, and at the same time they are leveraging technology to the fullest, deploying digital tax regimes that require more transparency and responsiveness from businesses operating in and across their borders. No matter where companies are on their technological journey, those that want to prosper in the era of digital taxation must develop IT systems, processes, and workflows that can meet these new digital reporting demands and ensure accurate indirect tax compliance in the swiftly moving future ahead.

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