

## Closing the tax expectations gap: Perception is reality, and how to change it

Two companion surveys conducted in 2006 and 2007 by CFO Research Services in collaboration with Deloitte Tax LLP (Deloitte Tax) reveal an “expectations gap” between the participating companies’ financial executives and their tax departments regarding the results and value tax departments deliver. In a Dbriefs webcast presentation on April 16, 2008, Mark Lazzaro, Partner, and Stephen Day, Director, both of the Deloitte TMS–Tax Management Services practice, discussed perceptions driving this gap and how CFOs and other finance executives, including tax directors, can help narrow the divide. More than 700 financial executives attended the presentation and took part in a series of online polls related to tax value issues in their organizations. More than half of the attendees were non-tax professionals.

What is your role?	
Votes Received: 667	
External Reporting	15.3 %
Budgeting, Planning and Analysis	9.4 %
Tax	44.4 %
Treasury	1.6 %
Operations	7.2 %
Other	22.0 %

“The tax function is often perceived to be operating separately from finance and other corporate functions, leading finance executives to question the tax function’s ability to add strategic value,” Day said in opening the discussion. “Findings from the 2006 and 2007 studies offer helpful observations about what has led to this expectations gap and how to close it through effective management and investment.”

Day said he believes the gap began to widen during the 2002-2003 time frame as Sarbanes-Oxley legislation rolled out. “That was when many so-called, ‘back-office’ functions, including tax departments, came under increased scrutiny regarding internal

controls and basic stewardship functions moving them out of alignment with business goals and making it more difficult to contribute to strategic achievements. Improvements have been made since then, but more can be done,” he said.

Lazzaro pointed out that taxes are one of the largest expense items for any U.S. company. “The impact taxes may have on business decisions can represent a significant amount of money. On a positive note, however, taxes are manageable — and good tax planning can have a very positive impact on shareholder value,” he said.

Day and Lazzaro emphasized that tax contributes value to the company as well as specific projects in two key ways: 1) financial impact through tax savings and 2) risk management. Major initiatives offer opportunities to add bottom-line value if smart tax planning is embedded in initiatives e.g., supply-chain projects, research and development efforts, plant expansion, legal entity rationalization, mergers and acquisitions, etc. Business leaders should insist on up-front involvement by the appropriate tax professionals and hold them accountable for adding value through tax planning and risk mitigation connected to these types of major business transformation projects. Setting the expectation and creating accountability will help unlock tax value and begin to close the gap. This type of tax involvement is a two-way effort. The tax department should find information channels that provide early insight to major initiatives. Gaining access during the early “visioning” stages of these efforts will allow much more welcome involvement for tax professionals.

In the area of risk management, tax manages such large portions of both the income statement and balance sheet that internal controls and enhanced accounting procedures have become a key part of the tax professional’s role. Accounting for income taxes can have both significant and permanent negative impact. Studies show that most top executives view risk management as one of their highest priorities. Mindful of that, Day and Lazzaro noted that since 2003 one-third of all material weaknesses reported by public companies (causing negative impact on company market values) were tax-related.

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The presenters said an expanded role for tax can lead to a kind of “catch 22” situation. According to Day, “The tax function has a stewardship responsibility that can’t be ignored regarding compliance, internal controls, and filings. Accordingly, tax departments are shorter on resources in recent years, because tax professionals are increasingly deployed to deal with growing demands of new accounting standards and corporate governance regulations. These realities make it tough to find time to ‘connect’ with the rest of the organization to do effective planning. Nevertheless, it is in the best interest of the business that they not allow themselves to be segregated from the decision making.” In an online poll, Dbriefs webcast attendees indicated they were divided with regard to perceptions and related roles of their own tax functions within the company.

### Which statement best describes your organization’s perception of the tax function?

Votes Received: 687

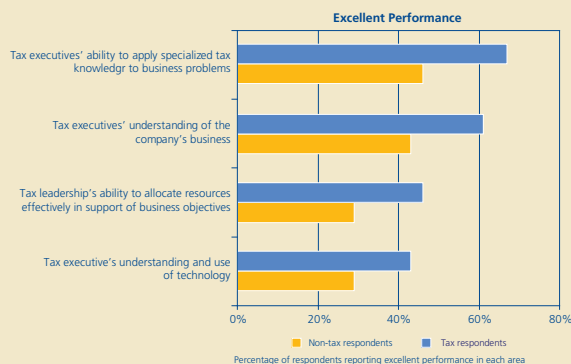
A cost center focused on complying with tax laws	33.8 %
A cost center to deal with the inherent risk of the tax areas	20.7 %
Specialists to be called in for specific topics	17.5 %
Value drivers to be included in business decisions	28.1 %

The surveys performed by CFO Research Services in collaboration with Deloitte Tax found that tax executives want to contribute more and their peers in finance want to get more from tax as part of the overall business decision-making process.

In order to meet these increased expectations, tax executives and business leaders will need to modify their own behaviors and companies will need to step up investments in new systems and processes, according to Day and Lazzaro. Tax executives, for example, will need to be more assertive in getting their departments involved in operations and transaction activities. And other executives will need to make room for tax input at the management table. This will not be easy because the research pointed out that some finance executives do not have confidence that their tax function is prepared to be a full participant in the business. Interestingly enough, the 2007 survey, “[Driving a More Valuable Contribution from the Corporate Tax Function](#),” also shows that tax respondents see themselves as having much more to offer than is currently being achieved by the function.

## Survey Findings

- Tax executives have a more favorable view of tax function performance



In contrast to CFO Research survey results, the results from the polling question during the April 16 Dbriefs webcast indicates that more than 70% of the more than 700 participants believe their tax professionals understand the strategic business issues.

The CFO Research 2007 survey results indicated that finance executives, in particular, view their tax peers as too focused on tax technical matters and not centered enough on business leadership. This “disconnect” was highlighted when tax and non-tax professionals responded to the question: To what extent will your company focus on the following activities as a source of business value over the next two years?

Finance executives believed the focus would be more on organic growth within current markets while tax executives saw M&A-type activities as receiving greater focus.

Additionally, in a separate and recent study Deloitte Tax conducted regarding reasons for material weaknesses and tax-related restatements, “a lack of personnel or untrained personnel” and “insufficient review or lack of review” garnered 55% of responses. Given these insights and disparities, tax executives need to improve their leadership, managerial, and people skills in order to interact more effectively with business managers and become integral parts of the decision-making process.

### Do the tax professionals in your organization have a clear understanding of business drivers and strategic direction of the company?

Votes Received: 701

Yes	72.9 %
No	27.5 %

Smart companies are working to even out this understanding from both ends — making investments in resources that allow tax executives to get to the decision-making table more often and requiring other business leaders to engage the tax perspective on the front end of key initiatives.

### In your opinion, what is the greatest impediment for tax professionals in their attempt to drive value through tax savings?

Votes Received: 656

Lack of tax knowledge	7.3 %
Lack of tools for research, scenario modeling, etc	15.5 %
Lack of business data	39.9 %
Lack of understanding of the business	24.7 %
Other (please send a question with your point of view)	12.5 %

The reality is that tax issues are quite complex and how best to plan for them can be misunderstood along the management chain. Broad enterprise initiatives present an opportunity for tax to reduce effective tax rate, reduce tax-related financial statement risk, as well as operate more efficiently through executing the initiatives in a tax-aligned approach. This opportunity requires tax executives educating themselves about a wide range of business issues that bridge the interests between finance and tax functions as well as operational groups.

It was noted that today's tax department leaders often don't have a "second-tier" level of managers reporting to them with the leadership, management, and communication skills to operate the department without significant involvement by the leader. This situation contributes to a lack of time and focus for the chief tax officer to take a more proactive role at higher levels of the organization; they are simply too busy running the day-to-day operations. Many tax professionals will also note that career development emphasis and rewards have mostly focused on tax technical knowledge, thereby discouraging pursuit of broader business strategy and management skills.

"Collaboration is difficult, but it's worthwhile," Day emphasized. About one-third of the webcast participants see their tax function adding value through planning and strong decision making. This is a positive result. But if you combined the three key stewardship roles of tax (Tax Compliance, Financial Close, Audit Defense), nearly 50% of the respondents to the polling question viewed these areas as Tax's primary value proposition. Day pointed out that this is a common view in today's environment and a driver to under-delivery of tax value.

### What is the area that your company's tax function currently adds the value?

Votes Received: 591

Strategy & Execution	8.3 %
Regulatory Compliance	24.4 %
Cash Management & Tax Payments	5.2 %
Closing Tax Entries, Tax Provision, Internal Controls	19.5 %
Risk Management & Audit Defense	5.9 %
Tax Planning & Tax-Efficient Business Decisions	36.9 %

In the final analysis, Day and Lazzaro noted, it will be up to tax executives to do all they can to connect effectively with their peers and with the business. Significant opportunities exist to create value. Do your part to make sure tax-aligned operations are contributing to business support and shareholder value.

## Driving Enterprise Value

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