



Tax data management
A foundation of sustainable
tax compliance, planning,
and examination support



One of the biggest challenges for tax departments today is maintaining and being able to quickly retrieve critical, tax-relevant data and documents for tax authorities during examinations. What steps can you take to improve tax data management in order to strengthen audit defense activities, streamline tax compliance, and support tax planning?

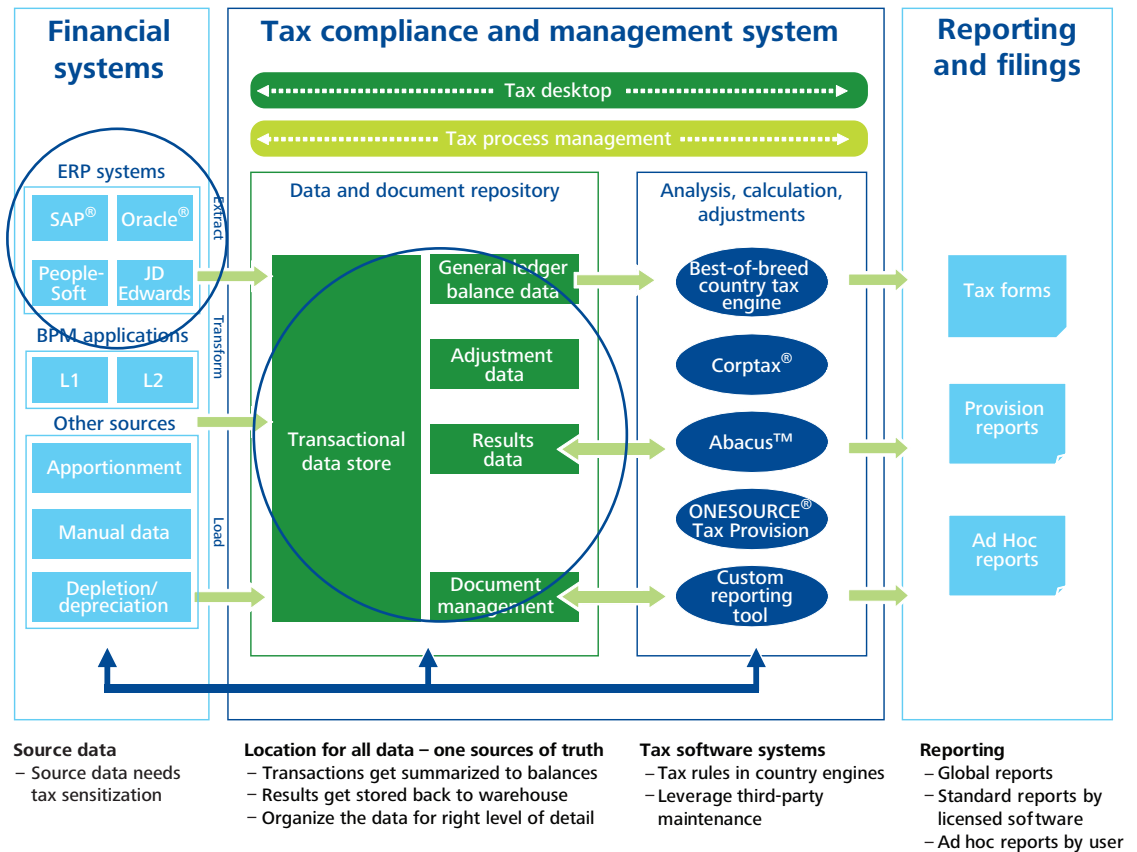
Deloitte hosted a [Dbriefs](#) webcast to discuss leading practices for data archiving and existing approaches for various enterprise resource planning (ERP) systems. Tax Management Consulting (TMC) Director John Myers and Tax Controversy Services Director Cindy Shubin addressed key distinctions between operational data archiving and tax record retention, sustainable practices for data and document retention, and trends in electronic records management. Nearly 1,600 participants shared their own views through responses to polling questions posed during the webcast.

Tax data management and the record-to-report process

Two elements of the record-to-report process (illustrated below) are particularly relevant to tax data management: tax data captured within the ERP systems (circled on the left side of the diagram) and tax-sensitized data stored for computation and adjustments by other systems (circled in the center).

Within the data store, tax-sensitized data from enterprise systems resides with data derived from downstream systems such as provision, compliance, and specialty tax software. In some cases, all of this data is centralized — perhaps in a data warehouse. More commonly, though, the data resides in a variety of tax data stores that companies organize and access using a third-party workflow or a variety of process management tools. These tools appear across the top of the diagram.

Evolution of tax function’s adoption and use of technology



As used in this document, "Deloitte" means Deloitte Tax LLP, a subsidiary of Deloitte LLP. Please see www.deloitte.com/us/about for a detailed description of the legal structure of Deloitte LLP and its subsidiaries. Certain services may not be available to attest clients under the rules and regulations of public accounting.

Complex tax record retention requirements

A quick look at several U.S. federal rules provides a flavor for the complexity of [tax record retention](#) requirements.

Under Internal Revenue Code (IRC) Section 6501(a), the Internal Revenue Service (IRS) must generally assess tax within three years of the tax return filing date or the unextended due date of the tax return in the case of a taxpayer that files an early return. Under IRC Section 6502(a), the IRS has 10 years after the assessment to collect the tax; therefore, if a taxpayer has a dispute with the IRS about an uncollected assessment, the taxpayer will need to retain those relevant tax records for a much longer period of time. There are numerous exceptions to the general rules however, including, but not limited to substantial omission of gross income, no return filed, net operating loss (NOL) carrybacks, and NOL carryovers.

In the case of income taxes, omission is calculated based on the amount of gross income reported on the return. If a taxpayer omits from gross income an amount in excess of 25 percent of the amount reported on the tax return, under IRC Section 6501(e), the statute of limitations for assessment will expire six years after the return is filed, rather than three years. If a taxpayer fails to file a tax return at all, IRS Section 6501(c) provides that the assessment period won't begin to run until the taxpayer actually files a late return.

Under IRC Section 6501(h), the statute of limitations for assessing a deficiency attributable to a carryback claim does not expire until the later of the limitations period for the loss year or the limitations period, for the carryback year. Essentially, this allows the IRS to audit the carryback year after the limitations period for that year ordinarily would have closed in order to determine if there are offsets to the loss amount carried back to that year.

In contrast, there is no IRC Section 6501 provision dealing directly with NOL carryovers. The general rule is that a NOL carryover creates a future tax deduction under IRC Section 172(a) in the year (or years) that the loss is used by the taxpayer to offset otherwise taxable income. The taxpayer must be prepared to support that loss deduction claimed on the later tax return year(s). In addition, the IRS can make adjustments to the available NOL deduction or credit carryover to an open year by making adjustments to an intervening barred year, thus increasing the amount of NOL or credit used in that barred year. These adjustments or offsets will operate to reduce or eliminate the amount of the NOL available to be carried to the open year. Therefore, if a taxpayer has NOL carryovers, the taxpayer will need to

retain its supporting tax-relevant data and documents for many years longer than the normal three-year statute in order to support those NOL deductions.

IRS Rev. Proc. 98-25 specifies the basic requirements for "machine-sensible records" that the IRS considers essential to support tax return filings. Two key requirements are that records must be capable of being processed and must contain sufficient transaction-level detail and not merely summary-level detail of the balances. "Capable of being processed" means that the IRS has the ability to retrieve, manipulate, print on paper, and produce output on electronic data. Note that there is no requirement for a taxpayer to create new machine-sensible records solely for the IRS that weren't created in the ordinary course of business and aren't needed to establish return entries.

What happens if a taxpayer isn't in compliance? While many taxpayers are most concerned about potential penalty assessments, a deduction disallowance for inadequate records may pose a bigger financial risk. Noncompliance carries the potential for summary IRS assessments, as well as penalties, such as the accuracy-related civil penalty under IRC Section 6662(a), the willful failure criminal penalty under IRS Section 7203, and the information-reporting-related civil penalties under IRS Section 6721.

It is worth noting that many states follow the IRS's lead and require taxpayers to provide transaction-level data to support their state filings on issues such as apportionment. Many states also require electronic, transaction-level data to support sales and use tax filings. In addition, many other countries have taken the same approach to tax examinations as the United States by requiring taxpayers to retain their machine-sensible information in electronic format and to provide that transaction-level data electronically at the time of examination.

Operational data archiving versus tax record retention

Archiving is the process of moving data from a "live" system or database to another storage medium. Companies archive data for a variety of reasons, but most commonly to enhance system performance (e.g., to improve access and search times or to reduce database memory issues and the time required to back up data). Archiving also can ease system management by reducing maintenance frequency. Data archiving typically involves only business-complete transactions, which can present issues with reconciliation, and the data may not be easily accessed once archived. Although there are some standard ERP retrieval tools that enable access to archived data, users in many environments still may require assistance from the information technology

(IT) department to access the data they need for audit support.

Tax record retention for financial data relies on a completely different concept. Unlike archiving, it doesn't take data out of the production database; rather, it is the process of extracting an exact copy of the tax-relevant financial information from the ERP to meet statutory and regulatory tax record retention requirements. Because extracted data files still reside in the online ERP database, even after the original data is subsequently archived, tax department users can retrieve data from extracts with query tools, including third-party software tools, and without further IT involvement. A tax data retention solution typically employs flat files, such as a comma-delimited text file; however, companies may choose to employ enterprise business intelligence tools as well. Users can extract reconciled data, and use third-party analytical tools or even Microsoft Excel to view or analyze the data.

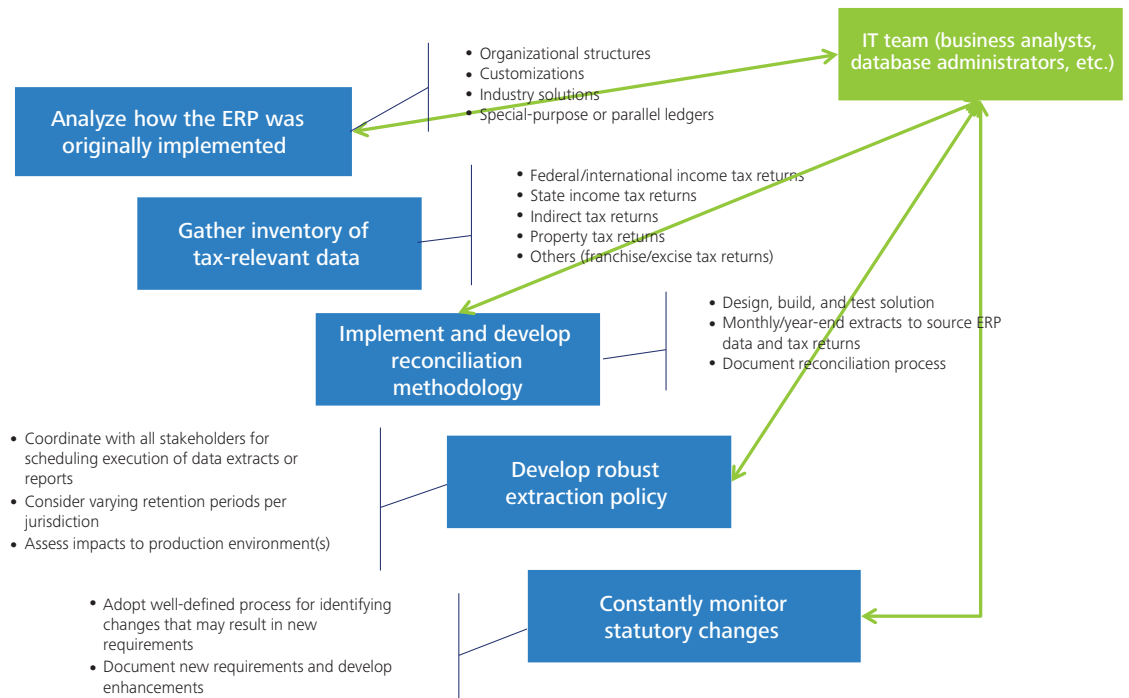
A tax record retention solution should be implemented before archiving to make sure the taxpayer has reconciled transactional data readily available to support audits and that the organization does not have to spend significant time searching for and reconciling archived (and potentially

incomplete) data once tax authorities begin to issue information requests. Once that tax record retention solution is in place, it is important to keep an eye on any tax-relevant changes made to the ERP system, such as new fields or new tables, because those ERP changes may result in necessary modifications to the extract solution.

The illustration below outlines an effective approach for tax record retention, beginning with looking at the original ERP implementation and any customizations, along with organizational structures and what those mean for the tax function. The next step is to gather an inventory of tax-relevant data. The best and probably easiest way to do this is to start with the data historically required to support tax audits. Once a taxpayer has defined tax requirements, the organization can create and implement a reconciliation methodology, develop the extraction policy, and, finally, monitor the solution continuously for changes. Coordination with business analysts and data administrators is vital throughout all of these steps.

SAP® provides its standard Data Retention Tool (DART) at no incremental cost for users with SAP® ERP Financials. DART transforms database objects into flat files that can be read by any software designed for flat files. It extracts

ERPs and tax data management: High-level plan



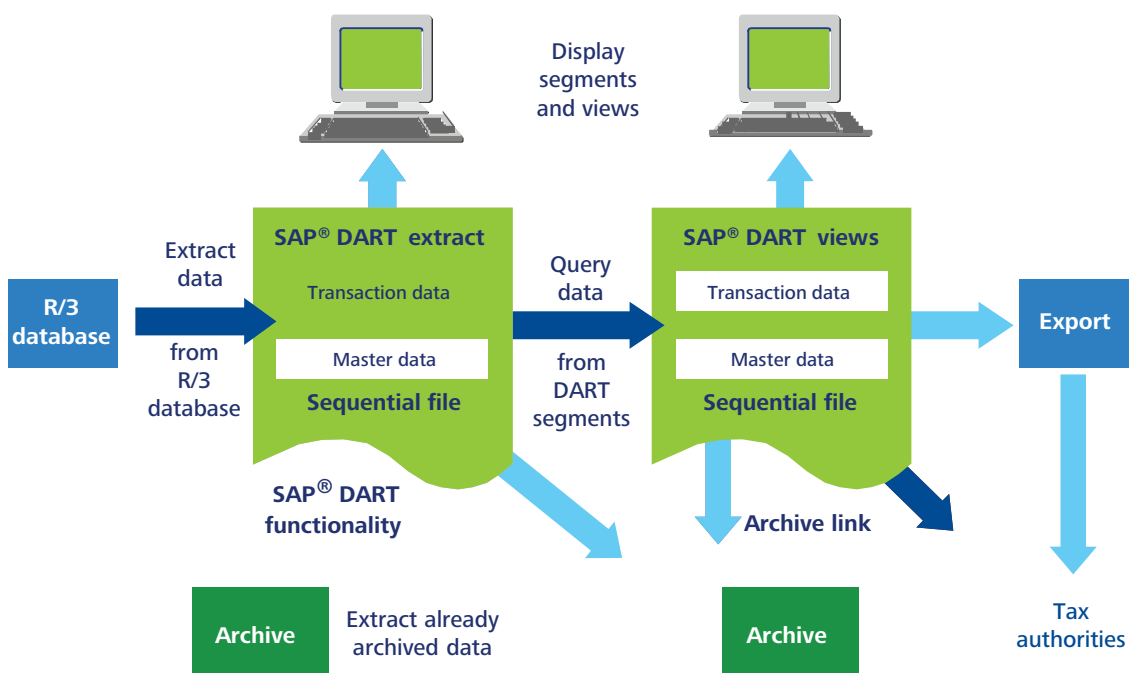
both the master and transactional data from standard SAP® fields and tables commonly required to support financial transactions, but it is not all-inclusive or plug-n-play and nearly always requires customization; it is important to gather and document all material tax requirements before putting a record retention solution in place such as DART.

The illustration below depicts DART’s moving parts. Once it is activated, DART takes certain data from fields and tables in SAP®, gathers them into segments, extracts them, and provides standard views of that data. Some companies use the DART Viewer and others just use DART’s basic functionality to extract the data and rely on another tool to analyze and/or view the extracted data. It is also not

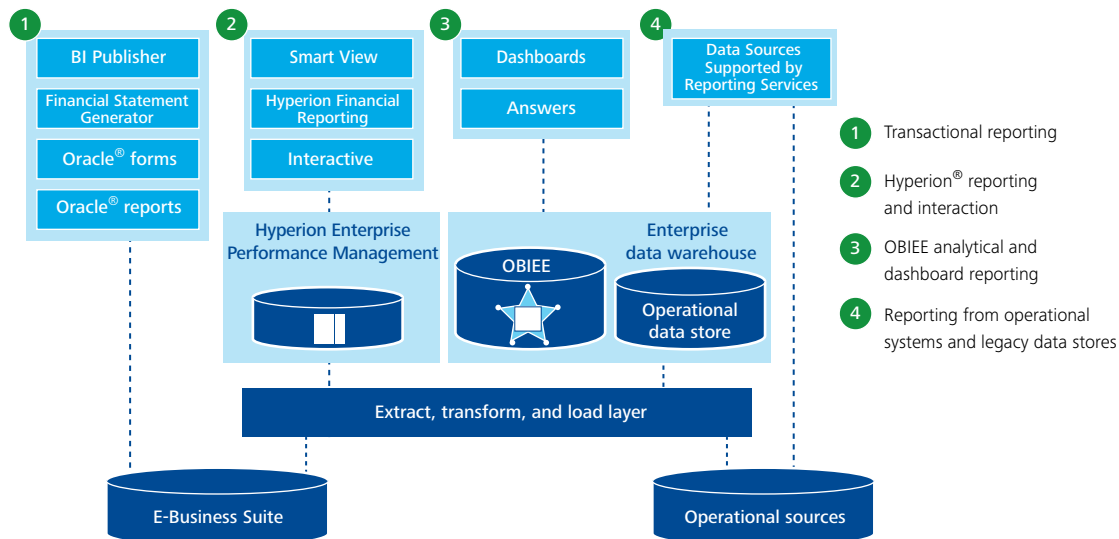
uncommon for companies to customize DART to add additional views of the extracted data.

Oracle® does not have a specific application akin to DART built for tax record retention, so tax-data retention requirements need to be incorporated into the overall system design. Oracle’s® Business Intelligence Enterprise Edition (OBIEE) platform is one solution that provides analytic and reporting tools to manage and report on tax-relevant financial data. Although it typically is used as a consolidation package, Hyperion® Financial Management is also a potential fit for accessing data and performing analytics. The diagram on the next page illustrates one possible tax record retention model for Oracle® users.

Tax record retention and SAP®



Tax record retention and Oracle®



Trends in electronic tax document management

Many tax departments are adopting tools that help them organize, digitize, and manage diverse pools of data. Tools such as Microsoft SharePoint® or tax-specific applications such as Corptax® Data Collect Workpapers and ONESOURCE® Workflow Manager have enhanced tax document management by allowing users to collaborate during the authoring, review, and approval of documents inside a tax portal. An electronic tax document management solution can help a taxpayer:

- Reduce the amount of time spent looking for documents.
- Eliminate the need to re-create documents when they can't be found.
- Enable document distribution on demand and reduce waste associated with printed materials.
- Reduce the cost of storing physical and unneeded electronic documents by deploying retention policies.

These solutions also can reduce risk through version control management features, use of consistent processes for managing documents, and established procedures for managing and creating the right documents.

Tax exam management across borders

Like their counterparts in the United States, global tax authorities face pressure to increase tax revenues without increasing tax rates. Accordingly, they are targeting resources toward high-profile, high-risk areas, such as transfer pricing, and taking a much tougher stance on what they deem to be tax avoidance. There also is greater cross-

border cooperation between tax authorities today, and we are beginning to see joint audits in which tax authorities from more than one country collaborate to look at both sides of transactions.

All of this is leading to greater tax risk globally, and yet many companies lack the infrastructure required to manage those risks. Global tax leaders regularly express concerns about their ability to:

- Minimize “fire drills” surrounding information requests
- Establish secure and audit-ready tax defense files that include the records produced by financial and operational systems.
- Manage a variety of risks associated with non-compliance, such as actual tax-dollar risks, material misstatement risks, reputational risks, and operational risks due to resource constraints.
- Share critical tax controversy knowledge on a timely basis within and across jurisdictions.
- Obtain readily available and visible status and analysis metrics for their domestic and global tax audits.

Automating the audit readiness and controversy management processes using a comprehensive Web-based solution can address these concerns. From a risk management perspective, this type of solution provides real-time visibility of audit issues and the related status and analysis metrics to parties who need to know while at the same time improving efficiency and effectiveness of global tax data and document management for audit-relevant information.

Perspectives of tax executives

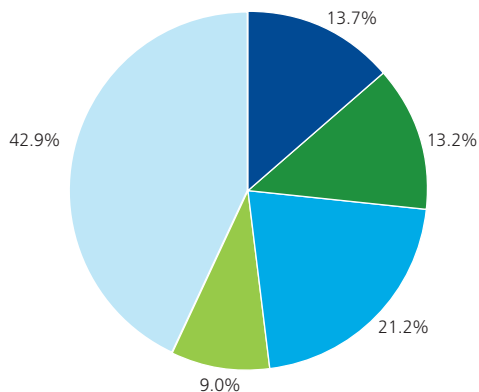
Deloitte hosted a [Dbriefs](#) webcast to discuss leading practices for data and document archiving and existing approaches for various ERP systems. Presenters John Myers and Cindy Shubin addressed key distinctions between operational data archiving and tax record retention, sustainable practices for data and document retention, and trends in electronic records management. Nearly 1,600 participants shared their own views through polling questions posed during the webcast.

Many companies archive enterprise system source data on a regular basis, primarily to improve system performance. Webcast participants were split with respect to awareness of these archiving schedules. About 27 percent said they receive notification about scheduled archives, with about

half of those in a more rigorous way. Another 30 percent said they receive no notice or hear about archiving only “through the grapevine.”

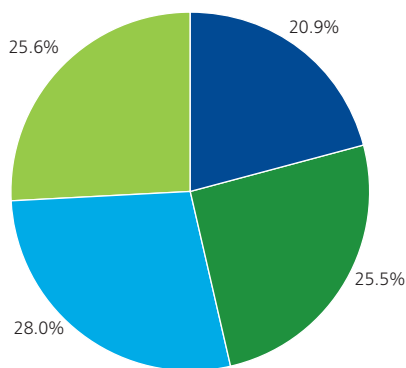
Tax record retention is critical to audit support, yet only 28 percent of participants said they have identified the data necessary to support audits and extracted it from source systems. Nearly half said they have not completely identified data in advance and extracted it from source systems to support audits: 21 percent indicated their organization’s strategy on tax record involves considerable time spent locating workpapers and/or retrieving/requesting electronic data on an as-needed basis, and 26 percent indicated they have limited electronic data available from financial system archives or the “live” system but require time to analyze and reconcile that data when requested.

Do you have a clear understanding of when and how the source data from your ERP system is scheduled for archiving?



- Yes, our IT department schedules specific meetings with the tax department to explain the timing and format
- Yes, our IT department notifies the tax department on the last day information will be accessible to allow us to download what we need
- No, I hear it through the grapevine when data will be pulled but do not know the level of detail
- No, detailed information simply disappears without warning
- Unsure/not applicable

Which statement below best describes your organization’s strategy on tax record retention?



- Considerable time spent locating workpapers and/or retrieving/requesting electronic data to support positions taken on returns on an as-needed basis
- Limited electronic data is available from financial system archives or the “live” system and provided to tax authorities as requested; time required to analyze and to reconcile available transactional data for completeness and accuracy
- Data necessary to support audits has been identified and extracted from source systems to support audits
- Unsure/not applicable

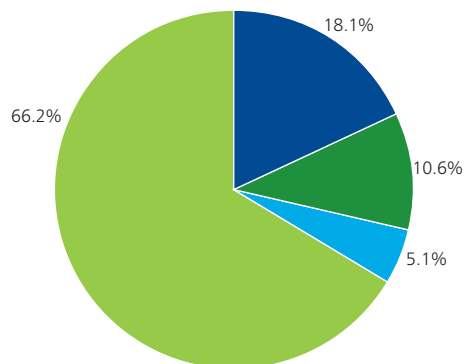
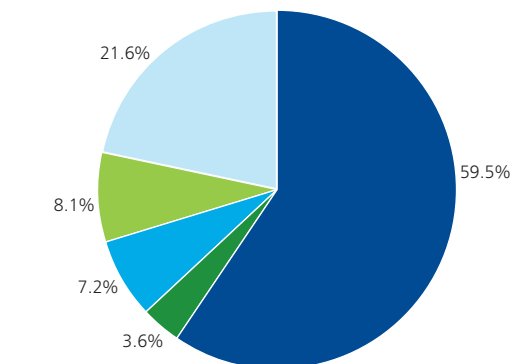
Source: Deloitte’s Tax Operations Dbriefs webcast, “Tax Data Analytics: Gaining Efficiency While Addressing Compliance,” held on March 15, 2012. Polling results presented herein are solely the thoughts and opinions of survey participants and are not necessarily representative of the total population.

As in many areas of tax management, spreadsheets continue to be the tool employed for managing data during an audit. Although there are general and tax-specific tools available to manage and track data flows during tax audits, nearly 60 percent of webcast participants said they rely primarily on spreadsheets, and another eight percent said they use hardcopy list(s). Just seven percent said they use a Web-based software system, while four percent use Microsoft Access® or a similar tool.

Electronic tax data management systems, including Web-based tools, can be valuable for many reasons. Webcast participants considered three key benefits and were asked to indicate the one most important to their organizations. Eighteen percent cited centralized electronic storage; 11 percent, version control features; and five percent, collaboration capabilities. The greatest number — 66 percent — said all three of those benefits are vitally important.

What is your company's primary tool for managing and tracking the dataflows during your tax audits?

Which benefit of an electronic tax data management system is most important to you?



- Spreadsheets (e.g., Microsoft Excel)
- Microsoft Access or similar
- Web-based software system
- Hardcopy list(s)
- Unsure/not applicable

- Centralized, electronic storage for documents
- Controlling version edits, updates, history, etc.
- Enabling collaboration among tax users
- All of the above

Source: Deloitte's Tax Operations Dbriefs webcast, "Tax Data Analytics: Gaining Efficiency While Addressing Compliance," held on March 15, 2012. Polling results presented herein are solely the thoughts and opinions of survey participants and are not necessarily representative of the total population.

Contacts

For more information on tax data management or Deloitte's Tax Management Consulting and Tax Controversy Services practices, email us at tmc@deloitte.com, or contact your Deloitte adviser or one of the individuals below:

Nathan Andrews

National Leader, Tax Management Consulting
 Deloitte Tax LLP
 +1 919 546 8055
nandrews@deloitte.com

John Myers

Director, Tax Management Consulting
 Deloitte Tax LLP
 +1 404 220 1346
jomyers@deloitte.com

Cindy Shubin

Director, Tax Controversy Services
 Deloitte Tax LLP
 +1 215 299 5252
cshubin@deloitte.com

For more resources that can help address the challenges tax departments face today, visit www.deloitte.com/us/movetaxforward.

This publication contains general information only and is based on the experiences and research of Deloitte practitioners. Deloitte is not, by means of this publication, rendering business, financial, investment, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. Deloitte, its affiliates, and related entities shall not be responsible for any loss sustained by any person who relies on this publication.