



Building supply chain resilience

**Balance business strategy and tax
efficiency for competitive advantage**



RESHAPING THE SUPPLY CHAIN

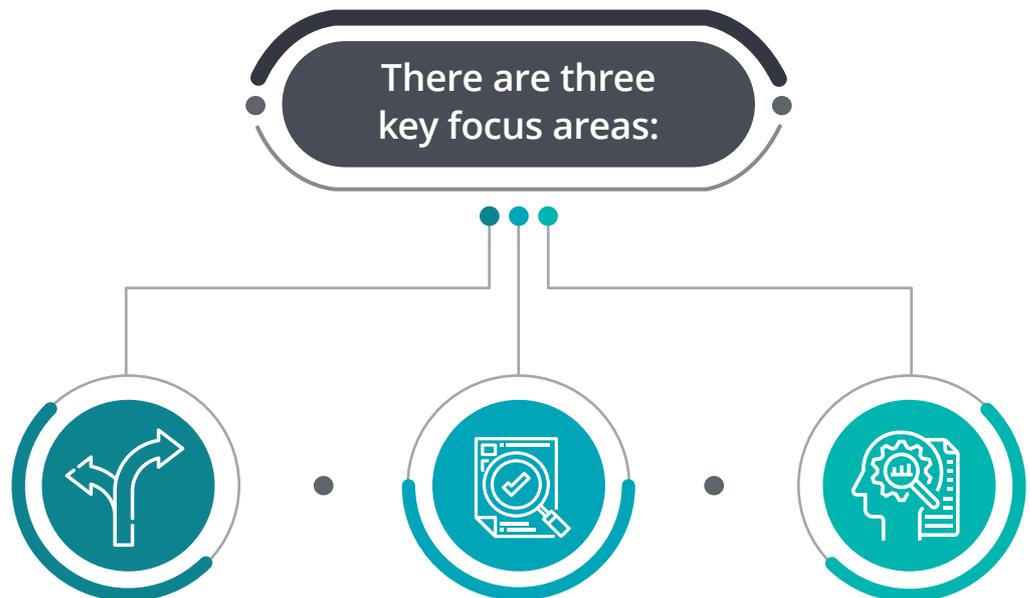
Building a resilient supply chain

The events of 2020 have highlighted how the interlinked, global nature of supply chains makes them vulnerable to a range of risks. Spurred by the COVID crisis, many companies are reconfiguring and refining their overall supply chain and risk management strategy, taking a more holistic view of potential risk and resiliency.

Looking into the future, business leaders are coordinating across their organizations to reevaluate the resiliency of their end-to-end global supply chains. This includes developing strategies that consider changes driven by technology and enacting new ways of working whether through the adoption of machine learning (ML), artificial intelligence (AI) or the future of work.

As business leaders weigh alternatives for sourcing, manufacturing, and distribution, tax efficiency is critical to maintaining profitability and shareholder value.

In this article, we examine how companies can reconfigure their supply chain strategies to build greater resilience and agility to quickly adapt to disruption.



- **Shift the global supply chain model**
 - Supply chain diversification
 - Digital transformation
 - Enabling the future of work in supply chain management and operations

- **Reconfigure for competitive advantage**

- **Assess the tax impacts of supply chain planning and transformation**

Shift the global supply chain model

Since 2020, nearly all companies have experienced some level of business disruption and many have been transformed forever. The impacts vary significantly by sector. The manufacturing sector, in particular, had to respond quickly to adapt to the crisis.

Manufacturing quickly adopted digital technologies and automation, and (depending on their location) rerouted where they source and manufacture their goods to bring production closer to consumer markets (nearshoring/onshoring).

Moreover, manufacturers with technological and digital capabilities (robotics, artificial intelligence, machine learning, drones, advanced analytics, big data, digital twins, virtual/augmented reality) showed an advantage in their ability to more quickly adapt in response to disruption. Some companies also transitioned from dependency on physical retail stores to digital or hybrid selling models to deliver their products.



**DIVERSIFY
RISKS TO
BUILD
RESILIENCE**

Supply chain diversification

Companies are seeking diversification of suppliers and geographies for sourcing raw materials and component products for better supply and capacity management, while at the same time focusing on cost savings, liquidity, and cash management. In addition, companies are seeking to address consumer concerns through more sustainable supply chains with ethical and socially responsible suppliers and practices.

For example, US President Joe Biden recently ordered a review of potential vulnerabilities in US supply chains for critical items from semi-conductors to pharmaceuticals to minerals. Many companies are also considering changes to their supply chains that would reduce lead times through acceleration of nearshoring or onshoring strategies. This shift can deliver both cost savings and efficiencies while maintaining a customer-centric focus.

However, the ability to adjust a supply chain can be limited by supplier capabilities including the availability of required materials or skilled workers in the desired jurisdiction. Environmental issues, local regulations, or tax incentives also may come into play. Decisions about how and where to modify a supply chain may ultimately depend on cost (including tax cost) and how much a consumer is willing to pay.

Supply chain transformations may involve moving supply chains away from certain countries (with respect to suppliers and/or facilities) to mitigate supplier or trade risk.



**IMPROVE
SUPPLY
CHAIN
FLEXIBILITY
VIA DIGITAL
TRANSFORMATION**

Digital transformation

Business leaders realize that they can run aspects of supply chains remotely with digital solutions. Accelerated use of technology is requiring leaders to consider investments in enhanced digital capabilities, for example:

- Developing or adopting new or advanced digital technologies for better real-time data and information to facilitate better decisions and innovation.
- Incorporating automation within the supply chain to build efficiencies.
- Using virtual “control towers” to monitor suppliers and production for supply chain transparency and visibility.
- Adopting e-commerce or omnichannel fulfillment and delivery models.
- Implementing smart factories: With advanced connectivity and optimization techniques, plant managers and technicians are able to run and monitor entire plant operations remotely, automatically balancing sudden spikes and troughs in demand-supply patterns across multiple plants.



**THE SUPPLY
CHAIN OF
THE FUTURE**

Enabling the future of work in supply chain management and operations

The pandemic has caused the workplace, workforce, and the nature of work itself to undergo some dramatic changes. The notion of where work can be done (i.e., the workplace) will likely continue its move from a physical to virtual environment as organizations increasingly adopt tools for remote working.

These trends will affect the supply network. Many manufacturers are likely to spend more on data management capabilities aimed at facilitating remote operations and improving operational efficiency. For example, Norsk Hydro, a Norway-based aluminum manufacturer that experienced limited access to plant infrastructure during the pandemic, plans to expand its data capabilities to remotely run and monitor plant equipment for improved resilience.¹

Business leaders should view their operations with a critical lens, challenging the status quo of where and how work is performed, and who performs it and in so doing can enable greater benefit to the organization and its stakeholders.

¹ Angus Loten, “[Pandemic to jumpstart spending on data tools at manufacturers](#),” CIO Journal, June 2, 2020.

Reconfigure for competitive advantage

Staying competitive in this new business and economic environment requires new strategies and practices. Companies must reevaluate the resilience of their supply chains—from planning for potential disruptions within their current geographical footprints, to a full review and transformation of their end-to-end supply chain models. Synchronization of the end-to-end supply chain through technology is key to enabling better decision-making to reduce the risk of disruption.

Assess the tax impacts of supply chain planning and transformation

It is crucial that tax leaders are involved in the early stages to better assess the tax impacts of supply chain transformations. Success requires combining supply chain transformation with operational tax changes which means tax teams must have full visibility into the digital innovation and supply chain strategies and their impacts on operations, profitability, and asset values.

Resilient tax leaders should assess the direct and indirect tax consequences of proposed changes to their company's supply chains. Through value chain alignment—the process of integrating global tax strategy with business operating models—the tax department can provide business leaders with timely and effective input on the tax implications of supply chain decisions.



Impact to value chain

The taxation of supply chains depends on:

- The movement of functions, assets, risks, and relationships such as intercompany pricing along the legal entities within the chain relative to country tax rates and other factors
- How the supply chain is structured from a tax perspective
- The alignment of other value creators (e.g., new technologies, R&D) within the structure

Changes to supply chains require the reassessment of intercompany transactions, transfer pricing, and intellectual property (IP) values. Proper tax analysis involves the use of robust and scalable tax operating models and considers:

- The benefits of tax treaty provisions and rates
- The use of favorable tax and trade regimes (e.g., Mexico's maquiladora regime) and other local country incentives, including the cost/impacts of exiting an existing tax incentive agreement
- The tax impacts of moving or closing physical facilities and expanding a company's virtual workforce



Intellectual Property (IP) related tax implications

Given the changes in the global economic outlook, it is an ideal time for tax teams to review and reassess the business IP portfolio. Legacy IP may need to be revalued due to the economic impact of the crisis on future revenue streams. New IP such as the adoption of new digital technologies, new business models, or research and development (R&D) activities should be identified and valued.

Value chain alignment considers where IP is located and how it is captured efficiently for tax purposes, either as pure IP or, for example, through a digital center of excellence. This analysis must consider transfer pricing impacts, location of Development, Enhancement, Maintenance, Protection, and Exploitation (DEMPE) functions, and impacts of multilateral regulatory initiatives such as the OECD/G20 Pillar One and Pillar Two projects.

Where an organization is considering moving IP between geographies in response to operational changes, tax teams will need review the transaction structure by taking into account updated IP values, changes to value drivers, future growth expectations, and direct tax impacts of transitioning into a new structure. The availability of advance pricing agreements (APAs) or tax rulings in affected jurisdictions can provide greater certainty on intercompany transactions and tax treatments.



Creation of new business models

The tax impacts of supply chain planning should consider whether new businesses have been created, such as where a company that sells products adopts new technologies or generates new revenue streams (maintenance, new service offerings, etc.), and whether these new businesses are subject to different tax or transfer pricing rules. For example, have digital innovations caused a company in the chain to provide an intercompany service in addition to selling goods? If so, how is the service valued and taxed?



Indirect taxes

Tax teams will need to focus on ensuring their company's ability to recover value added tax (VAT) to optimize cash flow, taking into account the rates of VAT in the different jurisdictions, as well as the rules for input credits and refunds of overpayments. Companies that are not VAT registered—or that delay VAT registration—can incur cash flow delays and related costs if they are not able to recover credits and in some jurisdictions, governments do not allow cash refunds of VAT. Efficiency in VAT administration can reduce costs and

is especially important in countries that may temporarily increase VAT rates to address immediate raising revenue needs. Depending on the jurisdiction, tax analyses also should consider the consequences of other indirect taxes such as goods and services tax (GST).

Changes to intercompany transactions and the geographical flow of goods along a value chain may impact the rates of customs duties and where those duties are paid. Tax teams will need to identify rate changes as well as opportunities to reduce global trade costs. These opportunities may include (where available) free trade agreements, including the recently concluded US-Mexico-Canada Agreement (USMCA) and the Regional Comprehensive Economic Partnership (RCEP), which is a free trade agreement among certain Asia-Pacific countries, as well as bonded warehouses, free trade zones, duty refunds, and similar programs. The effects of transfer pricing changes on the valuation of goods for customs tax purposes should be considered.

Additional administrative requirements, such as registrations, invoicing, and updating the importer of record should be factored in early in the process as possible.



Other considerations

Tax departments should work with their company's business and legal teams so that intercompany agreements accurately reflect the movement of supplies and associated value, including intercompany payments, through the chain. Coordination with the company's financial, treasury, and IT teams on financial reporting, invoicing and payments, inventory valuation, and required changes to internal systems, is required to capture accurate reflection of legal entities and intercompany transactions.

Take steps to build resiliency

According to [Deloitte's 2021 Global Resilience Report](#), 6 in 10 Chief Operating Officers believe disruption on the scale of 2020 will recur in the future on either an occasional or regular basis. That's why it's critical for businesses to build supply chain resilience and implement business strategies that accelerate performance and mitigate risk.

Resilient tax leaders need to focus on three key areas:

1



Provide their business leaders with timely and effective advice on the tax implications of supply chain decisions. To do so they need to understand their company's end-to-end supply chain and collaborate across their organizations to create value.

2



Participate in rethinking a businesses technology strategy as a means of driving increased innovation and agility at lower cost and faster speed to market.

3



Take an active role in planning and designing for their organization's future of work—particularly with respect to identifying areas for automation within the supply chain, and determining where and how to redeploy (and upskill) the workforce, and what skills and capabilities they'll need to set themselves up for growth.

Doing so will provide more strategic value, enhance resilience and empower organizations to invest in the right capabilities from technology to operating models to outperform their competition and operate boldly.

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