As the globe turns, so does the axle of tax compliance

It's important to have a strong working knowledge of the obstacles to tax compliance. Pawel Smolarkiewicz looks at how digital transformation is affecting organisations' approach

It is universally acknowledged that a global tax compliance strategy should be at the forefront of any SAP Central Finance project plan. Among SAP customers, however, tax compliance won't be a chief priority for everyone intending to transition to SAP S/4HANA, by the deadline of December 31st, 2025.

For these customers, this will prove a costly mistake. These days, businesses that neglect the compliance standards set by global tax mandates will find themselves faced with monetary sanctions, expensive audits, diminished cash flow, and broken relationships with suppliers and customers alike.

In fact, failure to comply could even destabilise SAP Central Finance and S/4HANA migrations altogether. In certain geographies, it can deadlock a whole company. To move forward, it's vital to understand that tax compliance must be non-negotiable for any switch to SAP S/4HANA, rather than being reduced to an afterthought or peripheral item.

It's fair to wonder how this might happen; the answer is that tax compliance must be approached as the axle around which the wheel of digital transformation turns. Consequently, it's important to have a strong working knowledge of the obstacles to tax compliance, which may have been overlooked in the past. In doing so, barriers to an organisation's ERP modernisation can be prevented, negating the risk of a wider roll-out getting derailed due to non-compliance.

Businesses seeking a successful migration will have to install an instance of SAP S/4HANA with the Universal Journal and SAP Landscape Transformation (SLT) replication server - the deployment model known as 'SAP Central Finance'. Once this has happened, facilitated by the prime benefit of SAP S/4HANA to run OLAP and OLTP workloads off the same systems simultaneously, businesses can begin transmitting data from other sources.

Moreover, methodically transitioning businesses process from legacy SAP and non-SAP systems minimises disruption to crucial business functions. Usually, this occurs in stages, over months or years, depending on how complex a company's legacy system landscape is; the legacy systems are retired gradually, as - in time - they become redundant to contemporary SAP S/4HANA capabilities.

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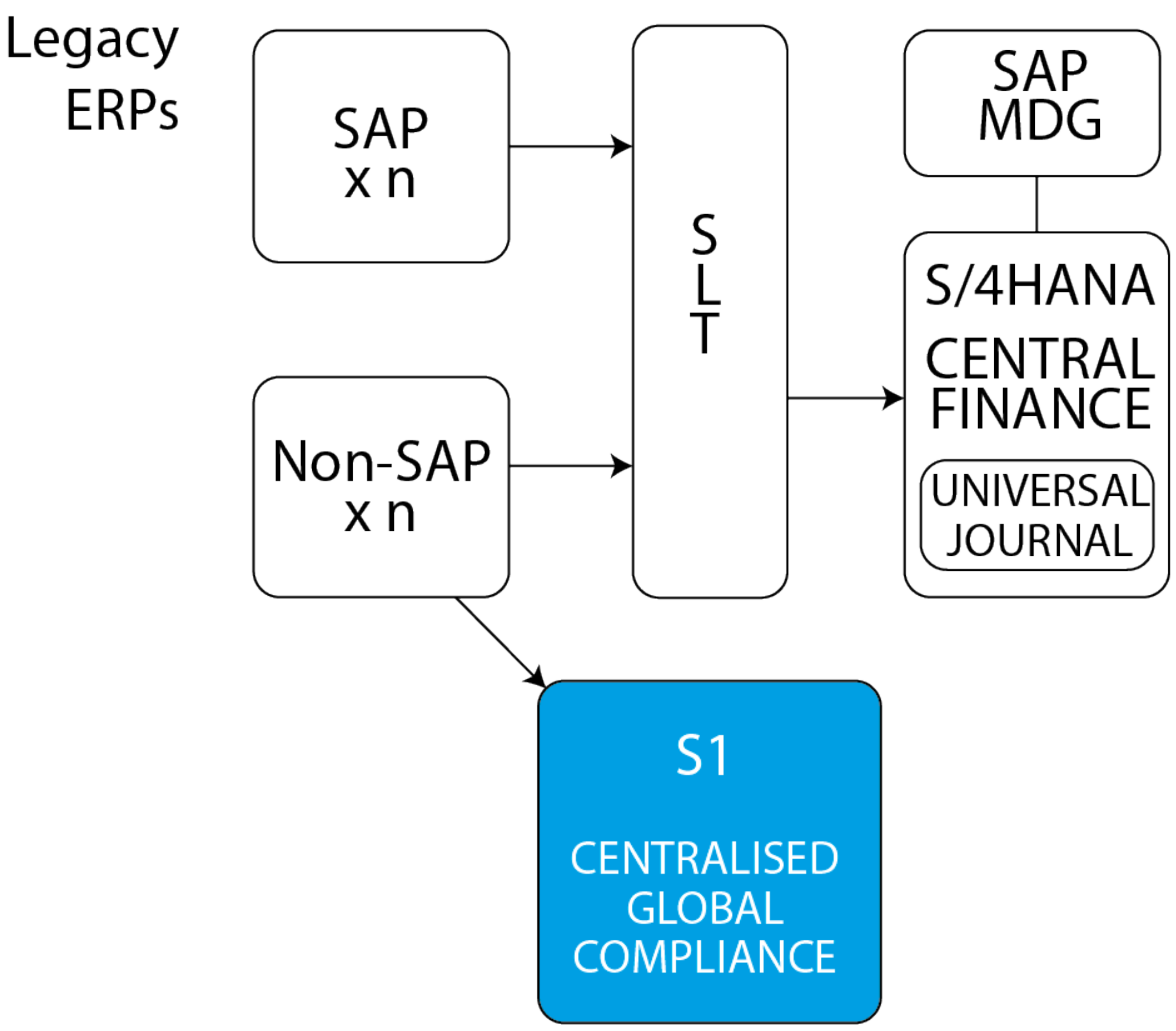
Tax and SAP S/4HANA Central Finance: a digital revolution

Still, let's not forget that there's another potential roadblock to a successful SAP migration, lurking deep in the shadows of the operations of most businesses: the digital transformation of tax. Across the globe, governments are beginning their own types of digital transformation, endeavouring to regain billions in lost revenue by decreeing real-time tax enforcement, alongside fresh methods of detailed digital reporting.

This is having a tremendous impact on the plans compiled by countless organisations for SAP S/4HANA migration, especially through a staged Central Finance model. What's more, if it isn't, then that has to change - and swiftly. Modern society is equipped with the technology to enforce continuous compliance; as such, an increasing number of governments are playing a more direct role in every transaction a company makes, amending the taxation requirements any time they spot the chance for a strengthened grip on revenue.

After all, governments are not going to stop innovating any time soon, as they carry on making waves to



increase revenue or reduce the tax gap. If businesses don't keep up, the particulars of digital transformation - including those all-important risks and costs - will spiral out of control.

India and the impact of changing compliance on Core Finance migration

To this end, it's worth looking at the worldwide developments in this space. Recently, India took up the digital tax mantle - the latest country to join the global trend that originated in Latin America of digitally transforming taxation.

We are already seeing different versions of this in Spain and Hungary, as just two examples, and Italy joined them in January of this year. Infamous all over the world for its manufacturing reputation, India's new system could have lasting ramifications on countless global corporations with a footprint in the country.

India commenced its journey by establishing a new committee to interrogate the utility of e-invoicing in a bid to crack down on tax evasion under its Goods and Services Tax (GST) programme. Once established, a failure to comprehend the process - and, in turn, a failure to comply - could lead to financial sanctions, negatively affecting an organisation's cashflow and profit. Relationships with suppliers, customers, and authorities could also be in jeopardy.

This is why it's so vital to examine how governments are updating tax mandates and the consequences of these new measures - and, in turn, why compliance absolutely has to be central to any IT transformation plan. In a nutshell: if India's going to change its tax laws, global businesses in the supply chain need to be aware of this.

Fortunately, technology - especially cloud-based solutions - can isolate the risks linked with the continually-evolving changes in tax mandates and automatically include them 'as-they-happen' in ERP, and disparate systems, as well as in SAP Central Finance. This is paramount, as the contemporary digital financial core brings with it a fresh set of requirements.

Multi-national corporations must isolate their central systems from perennial regulatory disruption in order to adhere to compliance standards, irrespective of where or how often these mandates might change. Now, there's no doubt that this is the only way that they can carry on doing business in countries governments have made digital tax a priority.

Keeping up with compliance changes to avoid a Mexican stand-off

Another country worth examining as an example of why compliance is so central to digital transformation is Mexico, which has a clear mandate for keeping companies honest. Failure to comply with Mexico's e-invoicing mandate can bring business in the country to a complete standstill. Shipments end up sitting stagnant at ports and payments to suppliers are never fulfilled.

When selling goods and services into countries where continuous compliance and tax enforcement are becoming increasingly complex, digital transformation of a company's financial core is paramount.

Core financial systems must be protected, through flexibility, from regulatory disruption in order to meet compliance requirements, no matter where or how often mandates might change. Failure to do so will hinder a company's ability to do business in countries where digital tax is championed.

Of course, the Mexican mandate is subject to endless change. If a mandate such as the e-invoicing regulation in Mexico changes during a transition to SAP Central Finance and a business that has rendered compliance a mere afterthought is unable to adapt to it, the ramifications on cashflow and working relationships with suppliers could be colossal. As such, it's important to have an adaptable system that can react to new and changing mandates - a cornerstone of any migration to SAP S4/HANA.

The process begins with the e-invoice itself (known as a CFDI in Mexico). Previously a paper invoice, the government now requires electronic invoices in a standard XML format. Organisations doing business in Mexico must generate an electronic invoice in this format with all relevant information (tax ID number and description of goods, for example). Once submitted, the shipper receives a unique number called a UUID from the government; once this is generated, a company can ship its goods.

This all happens in real-time. Equally, businesses receiving invoices must validate them with the government, ensuring that the information on the invoice matches the information stored in a government database.

Once this is confirmed, the company can take delivery of its shipment. If it doesn't, the government has visibility of discrepancies and can delay the transmission of goods, in some cases penalising the business in question for submitting erroneous data.

Nonetheless, financial penalties are just one of the many consequences of non-compliance. Delayed or cancelled shipments can quickly lead to frustrated customers and lost revenue. From there, the tax implications themselves can cause headaches, with painful monetary repercussions to top it all off.

Here, as well, e-invoicing compliance is just the tip of the iceberg. An e-archiving mandate necessitates that companies must store their invoices in a specific format, as this is the only way that they can be prepared for electronic audit by the government at any time. The process of cancelling an invoice, only recently created and likely to change at some point, is both complex and critical for remaining compliant.

Mexico, then, illustrates how governments are mandating enforcement tactics such as e-invoicing and e-archiving to track VAT payments in real time, thereby eliminating fraud and errors that would previously have led to underpayment. This is why it's imperative, when transforming finance systems, to have an adaptable system capable of reacting to new and changing mandates - evidently, the risks of not doing so are not worth it.

The power of the cloud

This is where the value of a complete cloud-focused culture shift becomes clear. A connected, central, cloud compliance solution - backed by continuous support - can provide the isolation from digital tax regulatory change disruption that businesses require to carry out their IT migration unhindered. Of particular note, a centralised compliance solution perfectly complements the SAP Central Finance deployment model - or, in fact, any extended migration project.

To this end, cloud compliance solutions must offer the benefit of being able to address both legacy and digitally transformed systems at the same, with neither at the expense of the other - a non-negotiable capability for successful phased migration.

Bearing in mind the formidable scope of any such IT project and the sensitivity of the data involved for SAP customers moving to S/4HANA, it's most likely that tax compliance will start life on the periphery in migration plans - but this shouldn't be the case.

In order to engineer this with equal parts power and precision, trusted third-party technologies based in the cloud can enable the wheels to keep turning by foregrounding two systems for any transformation: the system for centralising finance functions and that for centralising compliance.

Notoriously, global tax mandates can be convoluted and are in a perpetual state of flux. On top of this, they can be invasive in a company's business processes - and the repercussions of failing to comply have been starkly highlighted.

Moreover, mandates come attached with the scope to disrupt migration plans, increasing cost and causing delays in the process. For companies that depend on being able to continue selling goods and services into geographies where continuous compliance and tax enforcement are becoming increasingly complex, digital transformation of the financial core is essential - enter cloud technology.

The best approach is for tax compliance to be managed fully in the cloud by a relevant vendor, as this yields continuous compliance updates, investment in maintenance, infrastructure, and innovation that brings savings - not only monetary but also resources, including time and staff.

This is because the delivery of regulatory updates is automated, negating the need for manual intervention every time regulations change. Additionally, there are no nasty surprises for CTOs in terms of an unknown point solution running custom code in another country and delaying their migration to SAP S/4HANA.

Cutting to the heart of tax compliance

It's always going to be the case that, as a subject, tax compliance lends itself much more seamlessly to conversation than execution - but that's no excuse to take things slowly. Undeniably, the roadblocks of transitioning to SAP S/4HANA will be demanding enough without having to contend with compliance in-house in tandem.

Outsourcing tax compliance to a third-party in the cloud can fix this, isolating systems from ongoing disruption while enabling IT leaders within a business to focus on other crucial steps in the SAP Central Finance to S/4HANA digital transformation journey.

To this end, SAP advises that tax calculations should occur outside the SAP Central Finance system, in a source system before reposting into SAP Central Finance. Here, again, a trusted supplier with a cloud-based solution can silo amendments to tax mandates and automatically include them in Accounts Payable (AP), Accounts Receivable (AR), and disparate ERP systems, as well as in SAP Central Finance, as a business migrates data to the new repository.

Ultimately, in an age of abundant forms of digital transformation, organisations should now approach national tax authorities as key stakeholders in their core business processes. To achieve this, they must keep up with differing formats and continually changing tax compliance requirements.

As a result, the switch to SAP S/4HANA with Central Finance combined with a central modern tax compliance solution should form a portion of every company's odyssey to solve tax for good - perpetually vanquishing compliance headaches. ■

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