Managing Tax, Employment, and Payroll Compliance in a Changing Environment

HOW SENIOR FINANCE EXECUTIVES ARE STAYING AHEAD OF SWEEPING REGULATORY SHIFTS

A report prepared by CFO Research in collaboration with ADP
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About this Report

In December 2012, CFO Research conducted a survey among senior finance executives at U.S. companies. Through the online questionnaire, we sought to understand how midsize companies are rethinking their employment, tax, and payment-related compliance activities as a result of the increasing volume—and growing complexity—of the regulatory requirements they face. We were especially interested in how such companies are managing to build increasingly robust compliance processes in an era when their budgets for doing so are, at best, growing just slightly.

We gathered a total of 100 responses from companies with revenues of more than $100 million a year, who work in a broad range of industries.

### Title

- Chief financial officer: 35%
- VP of finance: 17%
- Director of finance: 15%
- Controller: 13%
- EVP or SVP of finance: 9%
- Finance manager: 3%
- Treasurer: 3%
- CEO, president, or managing director: 1%
- Other C-suite executive with finance responsibilities: 1%
- Other: 1%

### Revenue

- $100 million – $500 million: 37%
- $500 million – $1 billion: 17%
- $1 billion – $5 billion: 24%
- $5 billion – $10 billion: 9%
- $10 billion – $20 billion: 6%
- More than $20 billion: 7%

### Number of full-time employees

- Fewer than 100: 3%
- 100-499: 13%
- 500-999: 13%
- 1,000-2,499: 23%
- 2,500-4,999: 15%
- 5,000 or more: 33%

### Industry

- Financial services/Real estate/Insurance: 15%
- Auto/Industrial/Manufacturing: 13%
- Public sector/Nonprofit: 9%
- Wholesale/Retail trade: 9%
- Health care: 9%
- Food/Beverages/Consumer packaged goods: 9%
- Chemicals/Energy/Utilities: 6%
- Business/Professional services: 6%
- Transportation/Warehousing: 5%
- Pharmaceuticals/Biotechnology/Life sciences: 5%
- Aerospace/Defense: 5%
- Media/Entertainment/Travel/Leisure: 3%
- Construction: 3%
- Telecommunications: 2%
- Other: 1%

Note: Percentages may not total 100%, due to rounding.
Establishing a Culture of Compliance

“How beautiful the strategy, you should occasionally look at the results.” —Winston Churchill

One of the simplest ways to measure whether your company’s employment-related tax and payment compliance program is effective is to take an inventory of what’s not happening.

After all, if the system is routinely identifying risks associated with non-compliance and notifying members of management so they can intervene before any consequences materialize, then the company has gone a long way toward helping to establish a culture of compliance. That said, the standards and internal controls that are helping to get the job done now—embedded in such areas as technology, training, and oversight—may not be suited to the multitude of compliance and enforcement challenges ahead. It’s not enough for companies to track and analyze actual regulatory changes; they must also monitor proposed regulatory changes, whether they originate from the U.S. (e.g., the Dodd-Frank Wall Street Reform and Consumer Protection Act) or elsewhere (e.g., the U.K. Bribery Act).

The absence of fines, litigation, and adverse publicity relating to non-compliance is no trivial feat. But in an economically volatile environment, employment-related tax and payment compliance must also be measured by the same metric that defines success in many other business functions: controlling costs by eliminating wasteful practices and minimizing risks.

As senior finance executives know all too well, corporations are facing one of the most challenging regulatory and enforcement environments in years. Unlike, say, R&D, investment in employment-related tax and payment compliance may provide very little visible value. Making these compliance processes more efficient and controlled means successfully mitigating risk and avoiding unexpected costs. Many payoffs, such as a boost in the public’s confidence, are difficult to quantify.

The drive for cost efficiency coincides with more-stringent reporting and disclosure requirements, increasingly vigilant scrutiny, and reduced tolerance for even minor infractions. It may not be enough to minimize violations anymore; companies now need to step back and assess any practices that contribute to employment-related tax and payment compliance risks. “Just staying abreast of changes in countries’ regulations and tax changes is a challenge,” says the treasurer of a media/entertainment/travel company with annual revenue of more than $500 million. “We probably need to spend more funds on information-gathering.”

Many senior finance executives probably feel the same way—up to a point, anyway. That point, to be specific, is often when the prospect of shelling out more money is mentioned. “Resources are our most urgent challenge,” says the vice president of finance at a pharmaceuticals/biotech/life sciences company with more than $10 billion in annual revenue. “Overhead resources have substantial reduction targets this year. We have a significant risk of missing deadlines, overpaying, underpaying, or overlooking errors due to fewer resources and poor IT infrastructure.”

“Just staying abreast of changes in countries’ regulations and tax changes is a challenge. We probably need to spend more funds on information-gathering.”
—TREASURER, MEDIA/ENTERTAINMENT/TRAVEL COMPANY
The tension expressed by those finance executives—figuring out how to fulfill expanding employment-related tax and payment compliance requirements with limited budgets—emerges clearly from a recent survey conducted by CFO Research, in collaboration with ADP, a leading provider of global human capital management solutions. Responding to an online questionnaire, 150 senior finance executives, employed by U.S. companies with annual revenues of more than $100 million, shared distinctive insights into the challenges of creating and maintaining a state-of-the-art employment-related tax and payment compliance program. Slightly more than half of respondents, 52%, anticipate that their company’s budget for these compliance activities will remain the same over the next year. About 40% expect their budgets will increase, but only slightly. (See Figure 1.)

Still, there’s a potentially hefty price tag attached to ignoring vulnerabilities. Left unaddressed, a small non-compliance problem can grow into an expensive and incapacitating distraction. “Penalties and interest for even small mistakes are large,” observes the vice president of finance at a manufacturer with annual revenues of more than $500 million, adding that “tax discrepancies in Brazil from 4-5 years ago have significantly impacted earnings in 2012.” The odds of keeping such a violation under wraps may not be as good as they once were. The Dodd-Frank Act, for instance, dangles a financial incentive in front of whistleblowers who reveal corporate shenanigans. It’s generally smarter, financially, for a company to have taken preventive measures before regulatory agencies make a costly discovery. The vice president of finance at a pharmaceuticals/biotech company with annual revenue of between $10 billion and $20 billion laments that his company “had to pay a significant fine (billions of Euros) to the EU related to bribery charges in the sales/procurement area.” And in the U.S., the executive adds, “We frequently live with the threat of an FDA shutdown due to poor documentation around FDA compliance.”

“We frequently live with the threat of an FDA shutdown due to poor documentation around FDA compliance.”

—VP OF FINANCE, PHARMACEUTICALS/BIOTECHNOLOGY/LIFE SCIENCES COMPANY

FIGURE 1. “In the coming year, I anticipate that my company’s budget for compliance activities will ____________________.”
Economic growth may have stagnated, but the bull market for new regulations has been on an incessant upswing since 2002. That was the year that the federal government enacted the Sarbanes-Oxley Act, a law aimed at putting an end to the fraudulent accounting practices that had been unearthed in the high-profile collapse of such entities as Enron Corp. and WorldCom. So far-reaching was the legislation that it helped spawn a Y2K-sized industry of compliance consultants. More recently, in 2010, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act, a regulatory overhaul on a scale not seen since The Great Depression.

In addition, the SEC has aimed its initiatives at protecting investors and codifying governance practices. State and local governments have also weighed in, redefining corporate obligations in such areas as workers’ compensation, sales-tax collection, and the withholding of employees’ wages. More than one survey respondent refers to the fact that the quickly changing regulatory environment has led to far-reaching shifts. For example, the executive vice president of finance at a $1-billion professional services firm mentions that a theft of consumer e-mail information led to “a complete re-evaluation of security and compliance procedures.” Its failure to comply with Japanese employment laws, says the CFO of a financial services firm with annual revenue of more than $500 million, has led to “a complete rethinking of future foreign growth strategy.”

Finance executives are well aware of their weighty burdens relating to employment-related tax and payment compliance. According to more than 80% of respondents, over the past two years the task of monitoring compliance rule changes has become either “somewhat more” (66%) or “much more” (15%) time-consuming for the staff at their company. (See Figure 2.) Within that same time frame, about 60% of respondents “somewhat” agree (47%) or “strongly” agree (14%) that “my company has been under pressure to respond to tax, employment, and payment-related regulations in increasingly shorter time frames.” (See Figure 3, next page.) One survey taker, who serves as vice president of finance at a health-care firm

One company’s failure to comply with Japan’s employment law led management to undertake “a complete rethinking of future foreign growth strategy.”

![Figure 2](image)

“Over the last two years, the task of monitoring tax, employment, and payment-related rule changes has become ___________ for the staff at my company.”

- 15% **MUCH MORE TIME-CONSUMING**
- 66% **SOMewhat MORE TIME-CONSUMING**
- 10% **SOMewhat LESS TIME-CONSUMING**
- 2% **MUCH LESS TIME-CONSUMING**

Note: 7% of respondents selected “Not sure.”
with more than $1 billion in annual revenue, says that a failure in the accuracy of the company’s W-2s was more daunting to fix than it ought to have been because “the short turnaround time to implement new federal tax changes was a problem—the window was far too short.”

But even the occasional employment-related tax and payment compliance challenge can be a debilitating distraction for finance leaders, many of whom have emerged from The Great Recession with a newfound prominence. Having navigated their employers through the credit crunch and economic downswing, they have surfaced as top-line thinkers, switching their focus from stewards of preserving value to catalysts for driving growth. As newly minted leaders who are repositioning their companies’ balance sheets for post-recession growth, they are eager to keep adding to their growing influence. As they battle uncertainty on so many fronts—from ever-evolving business models to the redefined role of the finance function itself—they can’t allow compliance issues to sidetrack them.

Nor can they afford to overlook the need to build a solid foundation for employment-related tax and payment compliance. Answering an open-text survey question about the most urgent challenge that their employer faces in monitoring and managing compliance with respect to employment-related tax and payment compliance regulations, a director of finance at a $1 billion-plus company in the consumer packaged-goods industry responds that his most pressing priority consists of “making an inventory of compliance requirements across all international operations so all requirements gain visibility and become easier to track.”

“Over the last two years, my company has been under pressure to respond to tax, employment, and payment-related regulations in increasingly shorter time frames.”

—VP OF FINANCE, HEALTH-CARE FIRM
That priority reflects a clear grasp of what it takes for a business to pass safely through the regulatory and enforcement minefield in which finance executives now must operate. In fact, about two-thirds of respondents say that employment-related tax and payment compliance is “one of several priorities” of theirs. And about one in five respondents identifies such compliance as “one of my top priorities.” (See Figure 4.)

In recent years, finance executives have grown accustomed to serving in much more proactive roles; they’ve gone from being responsible for ensuring the accuracy of financial statements to supplying insights that can help support decision making. Many finance executives aren’t making any exceptions for employment-related tax and payment compliance, either; survey-takers see the value in taking a more strategic approach to it. In fact, 43% of respondents agree that their company “would realize measurable benefits if it took a more proactive approach to compliance in the areas of tax, employment, and payment regulation.” However, this begs the question: Is it time well-spent?

Finance executives are devoting attention to their companies’ compliance processes. Virtually all survey participants report that they spend at least one day a week on tax, employment, and payment-related compliance. However, this begs the question: Is it time well-spent?

More than 40% of respondents agree that their company “would realize measurable benefits if it took a more proactive approach to compliance in the area of tax, employment, and payment regulation.”
The aim of an employment-related tax and payment compliance program is often deceptively straightforward: to create a culture consisting of practices that will help prevent misconduct and inspire desirable conduct—and whose effectiveness is ultimately measured by its ability to help detect problems and improve outcomes. Faced with an abundance of new and expansive regulations, and with their companies’ margins compressed (if not crushed) by the economic downturn, many finance executives haven’t had the luxury of building a compliance function from the bottom up. Instead, they’ve constructed the compliance puzzle piece-by-piece, adding the capabilities they needed one-by-one, as if they were unrelated tasks.

Together, the observations of respondents who answered our survey’s open-text questions create the picture of a disjointed effort with respect to employment-related tax and payment compliance, riddled with expensive outlays and lacking any coordinated attempt to optimize efficiency. Based on the survey responses, there’s little evidence to suggest that management has taken a comprehensive view of employment-related tax and payment compliance, working rigorously to determine how each practice can best be performed, while also identifying forthcoming needs and opportunities. As one CFO puts it: “Global tax compliance is spread across a very decentralized internal team and a multitude of outside vendors.”

One problem that results from this ad hoc approach to stitching together an employment-related tax and payment compliance program is the absence of any unifying platform or centralized system. Instead, data may be stored in multiple general ledger systems, making it difficult to integrate it into a standardized format. Staying in compliance turns ever-more cumbersome when the data is stored in a multitude of spreadsheets. An alternative: examine common business and processing traits across multiple regulations—to treat compliance as a strategic imperative and key to the growth of the organization rather than a series of unrelated tasks, or an uneven, costly activity with few tangible benefits.

The results of the survey conducted in collaboration between CFO Research and ADP suggest that employment-related tax and payment compliance activity tends to be pieced together, not designed holistically. In fact, 71% of respondents say that employment-related tax and payment compliance activity at their company “relies on multiple, separate information systems.” By contrast, just 5% of respondents say that such compliance activity “relies on a single, standalone system.” (See Figure 5, next page.)

And while 19% of respondents expect that the number of vendors their companies do business with will increase in the next two years, only 12% of respondents expect the vendor count to decrease during that time span. (See Figure 6, next page.)

By solving one challenge at a time, executives could end up with an employment-related tax and payment compliance program that is uneven. One controller says that his company’s compliance system has been shaped by chasing one problem
after another—“acquiring the needed expertise either externally or internally,” as the controller puts it. It’s a reactive approach that stands in stark contrast to “having a strategic company-wide risk plan,” as one director of finance puts it when characterizing his company’s most urgent compliance-related challenge.

Respondents say that internal involvement in employment-related tax and payment compliance is spread among various departments. The functions most frequently chosen as involved in such compliance include IT (79%), Operations (70%), Accounts Payable (66%), Human Resources (65%), Administration (64%), Finance (59%), and Treasury (56%). The remaining departments—including Corporate, Controller, Tax, and Legal—each hover at around 50%.

The fact that this employment-related tax and payment compliance activity is so broadly spread throughout the organization suggests that finance leaders have yet to look at it from a strategic perspective, figuring out how to best achieve sustainable cost advantages and assigning responsibilities to the most appropriate parties. Such a diffuse structure may make it more difficult for companies to identify—and improve—weak areas, while also increasing the challenges involved in, say, meeting deadlines and providing thorough documentation.

Faced with the accelerated pace of employment-related tax and payment compliance regulatory changes, and the growing complexity involved in managing risk, executives may spend too much time tracking these regulatory changes—and not enough actually managing the risks. Disparate systems and data sources, difficulty accessing or locating up-to-date information, and the ever-changing nature of regulations can combine to bury compliance-focused employees in data collection. What’s lost? The
time they need to review and analyze data, the performance of value-added activities—such as managing regulatory relationships—that gets crowded out by mandated duties (such as filings), and the opportunity to make progress toward retrofitting existing employment-related tax and payment compliance processes to meet modern demands by leveraging technology and adopting best practices in such areas as data collection and utilization.

As eager as they may be to follow their customers into new global markets, companies aren’t likely to get very far without having equipped themselves to meet new or unfamiliar compliance demands. Nearly 40% of respondents agree either “somewhat” or “strongly” with the statement that “it is difficult for my company to enter new geographic jurisdictions because of varying tax, employment, and payment regulations.”

One survey respondent, the controller of a company in the transportation/warehousing industry, describes the company’s foremost challenge in connection with employment-related tax and payment compliance as “understanding the complexities and requirements for state regulations when growing our customer base into new states.” Echoing such sentiments, the chief financial officer of a business operating in the areas of financial services/real estate/insurance reports, “Understanding foreign rules and regulations in order to grow markets outside the U.S. is a major challenge. The fear of violating rules that we do not know about inhibits growth possibilities.”

No matter which way they look—inward, toward domestic markets, or outward, toward the promise of international expansion—senior finance executives take in the same view: growth restrained by compliance demands. This is the same 150-member group which unanimously agree—well, almost, with 90% of them sharing a single view—that “contributing to organizational growth is one of my department’s key functions.” Clearly, they don’t want to let anything—including the compliance-related shortcomings of their own companies—stand in their way.

“Understanding foreign rules and regulations in order to grow markets outside the U.S. is a challenge. The fear of violating rules that we do not know about inhibits growth possibilities.”

—CFO, FINANCIAL SERVICES FIRM
Non-Compliance is Not an Option

Before starting a formal compliance program, it’s important for companies to take an inventory and make an assessment of their compliance risks. Executives can identify resources, both internal and external, that can help shorten the time required to correct compliance. The compliance culture needs to spread wider and reach deeper as the demands and challenges pile up.

Top executives need to keep pushing the compliance culture, whether it’s a first or another opportunity to showcase its benefits. One VP of finance describes his most pressing priority as “to gain top management support for compliance activities and to train a lot of people, recently hired.” What companies need is a sustainable, long-term compliance plan that helps strengthen controls, minimize costs, and ensure the accuracy of reporting. The money invested in technology may offer a return in the form of improved financial operations and reduced threats to financial integrity. Only 13% of respondents report that management has access to real-time, consolidated employment-related tax and payment compliance data through a dashboard or a technology platform.

But the strain on their systems is showing. Respondents do see the potential value in taking a more active approach to employment-related tax and payment compliance. In fact, 43% agree (35% “somewhat”) that their companies would “realize measurable benefits if it took a more proactive approach to compliance.” (See Figure 7.)

The changes senior finance executives see ahead include making employment-related tax and payment compliance less manual and adding automation to specific areas. But with their regulatory burdens ever-increasing, finance departments frequently face the prospect of extending their compliance-related functions. Layering on processes means adding costs in the form of bringing new hires aboard or buying complex measuring and tracking tools. Without the requisite training to operate such software and interpret the results, employees are likely to increase the number of compliance-related errors they make.

FIGURE 7. “My company would realize measurable benefits if it took a more proactive approach to compliance in the areas of tax, employment, and payment regulation.”

<table>
<thead>
<tr>
<th>Agree Strongly</th>
<th>Agree Somewhat</th>
<th>Neither Agree Nor Disagree</th>
<th>Disagree Somewhat</th>
<th>Disagree Strongly</th>
</tr>
</thead>
<tbody>
<tr>
<td>8%</td>
<td>35%</td>
<td>36%</td>
<td>12%</td>
<td>6%</td>
</tr>
</tbody>
</table>

Note: 3% of respondents selected “Not sure.”
A bulging error-rate may also result from adding more handoffs, which is an inefficient—if natural—response to the growing complexity of compliance. But every handoff is another opportunity for a delay or an error—as survey respondents already seem to know. (See Figure 8.)

With respect to such processes where they lack both internal resources and the appropriate skill set, finance executives may have no choice but to rely on external partners.

The cracks in employment-related tax and payment compliance are already showing. Companies may literally be paying a price for their failure to take a comprehensive view of employment-related tax and payment compliance. Respondents have clearly accepted—and adjusted to—the fact that they have to settle for incurring a substantial level of penalties. While one-third of respondents characterize the frequency of annual penalties they’ve incurred as a result of non-compliance as “few and far between,” the assessments of the rest range from “less than most of our peer companies” (25%) to “average” (19%) to “a little too high” (11%) and “much too high” (5%). (See Figure 9.)

Companies are clearly tolerating a level of inconsistency that they may not allow in, say, finance. Even a failure rate that is characterized as “few and far between” would seem unsatisfactory; management would be well-served by raising its expectations, recasting compliance to share some of the traits embodied in a well-managed finance function. Companies would likely benefit from a compliance function that is more predictive and one that is able to help anticipate lapses and correct them before the company incurs any penalties as a result of non-compliance.

For companies, the key is not to let their ultimate goal out of sight: manage the increased demand
for information to provide business insights and meet the expectations of regulators with minimum manual intervention. For example, banks and financial institutions today are facing a multitude of regulatory agendas and increasing levels of onerous compliance requirements by regulatory bodies and central banks around the world. Designed correctly, compliance programs should help prevent and help ensure that corporate activities are conducted in accordance with applicable criminal and civil law. By giving corporate leaders an integrated and holistic view of the impact of compliance activities on their businesses, a compliance program can help position the company for growth. And that can give senior financial officers just the opportunity they’ve been wanting.
Today’s businesses need an ally when it comes to managing the increasingly complex landscape of employment-related tax and payment compliance. In 2012 alone, there were 17,000 proposed tax rule changes across 10,000 unique tax jurisdictions, according to ADP internal data analysis.

With this volume of change, it’s easy to understand why CFOs, human resources executives, and finance executives find it challenging to effectively manage compliance and regulatory changes on their own. The time commitment can be overwhelming, consuming a significant portion of staff hours and interfering with more growth-oriented activity.

Armed with the right compliance platform, CFOs, human resources executives, and finance executives can help their organizations save time and money by maintaining compliance and mitigating non-compliance risk, improving business-process efficiencies and driving organizational growth.

With ADP SmartComplianceSM, a cloud-based unified platform of outsourced services that helps medium and large companies better manage key tax, employment, and payroll compliance capabilities, senior finance leaders are helping to reshape their employment-related compliance strategy by:

**Taking a Proactive Approach to Compliance** – Being proactive helps companies stay current with pending rule changes, increase the efficiency of day-to-day compliance management, and avoid penalties and fees related to non-compliance.

**Streamlining Systems and Investing in New Technology** – Reducing the number of touchpoints and handoffs in compliance processes can help increase efficiency and productivity. Implementing technology that is compatible with existing enterprise resource planning (ERP), human resources, or financial systems of record is essential to helping achieve maximum efficiency and return on investment (ROI) with minimum investment.

**Gaining a Truly Strategic View** – Using an integrated approach to compliance management helps provide executives with the comprehensive data needed to support critical business decisions, drive organizational growth, and improve business process efficiencies. Utilizing new technologies—such as dashboards—assists with the presentation of multiple data streams from disparate systems into a single, actionable platform. Without a strategic view of real-time information, financial managers are left navigating a maze of information sources.

**Leveraging Outside Expertise** – Managing increased regulatory complexity will likely remain a key component of doing business in the future. Companies may need to devote added resources to forecasting new risks—a time-consuming task. Finding the right partner with the right level of compliance experience and expertise helps leaders to move forward confidently and with greater efficiency.

**Make Compliance Easy**

With ADP SmartComplianceSM, you have the tools to help achieve comprehensive employment-related tax and payment compliance and improve efficiency while contributing to strategic business growth. With ADP SmartCompliance, we can help you achieve these goals while using virtually any ERP, financial, or HR system of record.

For more information on ADP SmartCompliance, visit adp.com/smartcompliance or call 855-237-4236.

“We developed ADP Smart-Compliance based on feedback from our clients. They told us that the flexibility to complement existing systems was essential. One of the strongest components of this new platform is its ability to work with virtually any ERP, and we’ve developed partnerships in the industry to make that happen.”

—DOUG POLITI, PRESIDENT, ADP ADDED VALUE SERVICES