

E-Book

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# The paradigm shift in digital tax transformation

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Introduction: The paradigm shift in digital tax transformation	03
Digital tax administration overview	04
Digital reporting, analytics and exchanging information	05
The emergence of digital tax departments	10
Transactional data shifts driven by the digitalisation of VAT	13
The growing need for digital savvy tax professionals	14
The future tax professional	15
About VATBox	16

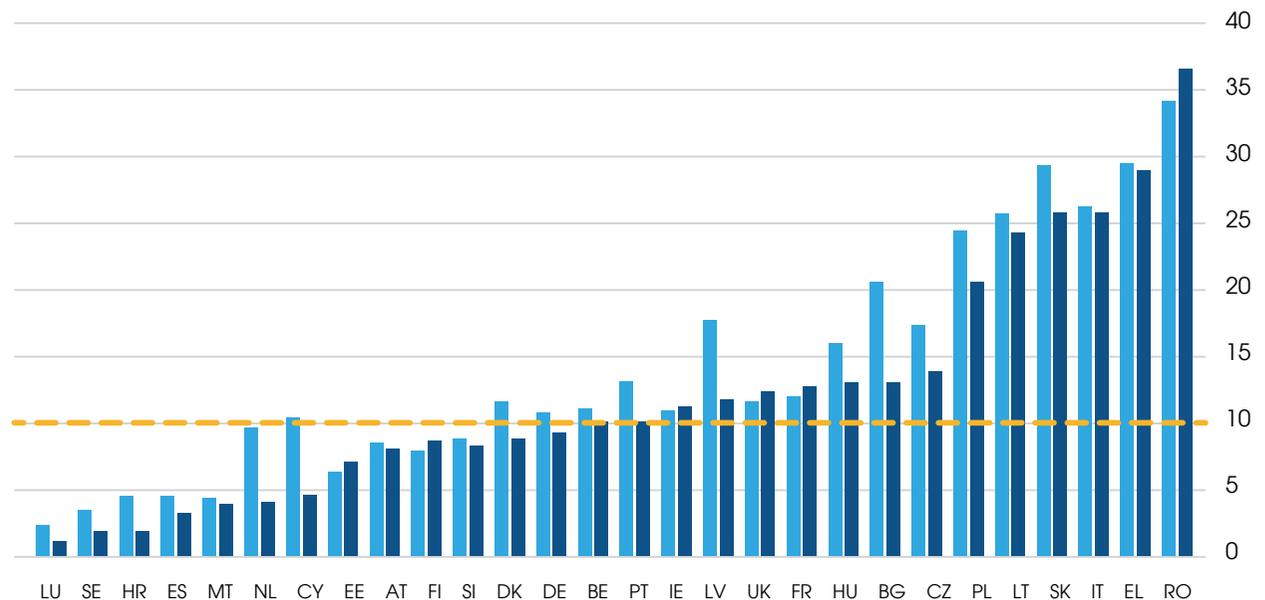
## Introduction: The paradigm shift in digital tax transformation

The tax landscape is changing at a rapid pace. Corporate Income Tax (CIT) is experiencing a major reform driven by the BEPS Actions<sup>1</sup>, which makes sense considering that CIT has been the most scrutinised tax for decades. Although BEPS Action 1<sup>2</sup> is all about challenges around digitalisation, it mainly touches upon the allocation of taxable income across countries, as opposed to the operational part of tax collection and management. So why should we care about the operational part as well?

This operational digitalisation is significantly impacting transactional taxes like VAT & GST (hereinafter referred to as VAT). In combination with the European Commission's efforts to close the **VAT Gap of EUR 137 billion**<sup>3</sup>, the digital transformation of VAT is a massive gamechanger for both tax administrations and corporate tax departments. The rapid developments of (digital) solutions to improve compliance and find the smallest anomalies in the data make it a very agile landscape from a VAT perspective.<sup>4</sup>

*In this eBook, we provide an overview of some key trends in the digitalisation of VAT, both from the tax administrations' and the taxpayers' perspectives.*

VAT Gap in the EU-28 Member States, 2018 report



<sup>1</sup> <https://www.oecd.org/tax/beps/>

<sup>2</sup> <https://www.oecd.org/tax/beps/beps-actions/action1/>

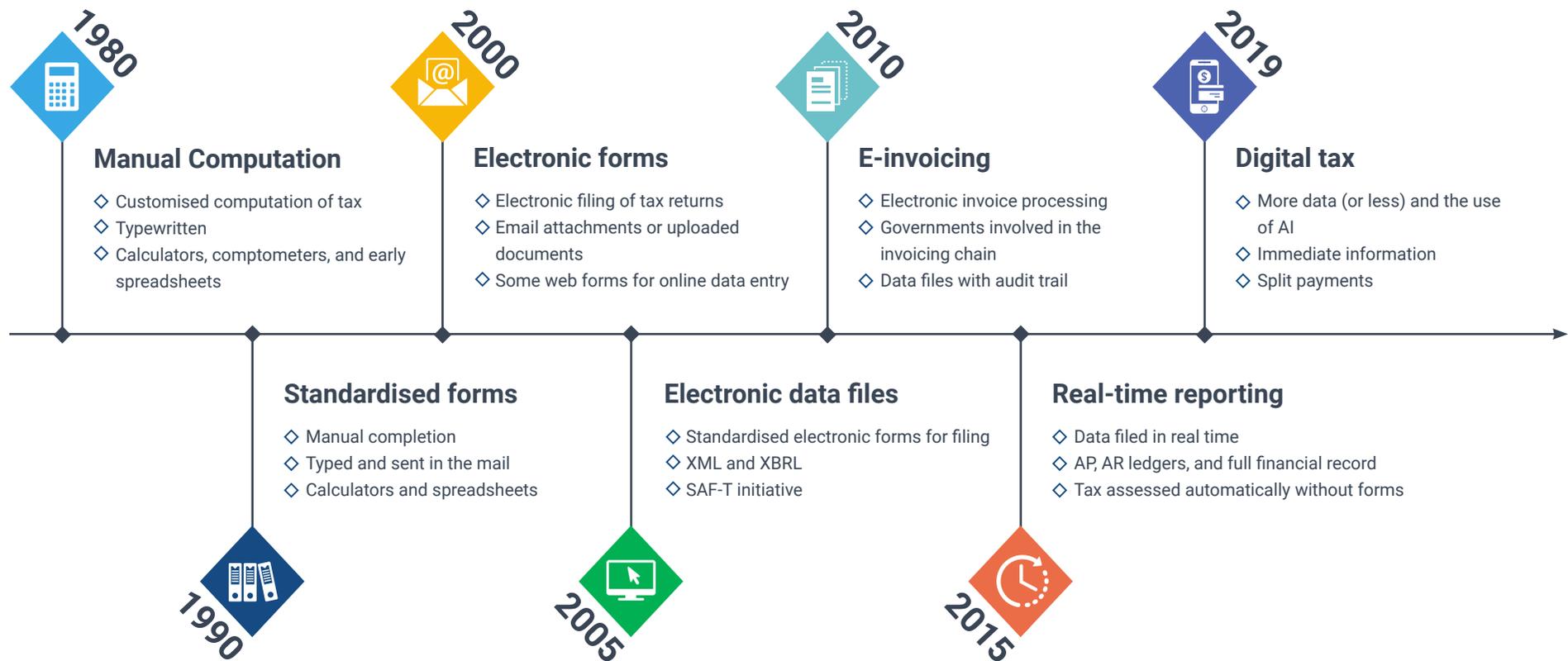
<sup>3</sup> [https://europa.eu/rapid/press-release\\_IP-19-5511\\_en.htm](https://europa.eu/rapid/press-release_IP-19-5511_en.htm)

<sup>4</sup> [https://ec.europa.eu/taxation\\_customs/business/vat/action-plan-vat\\_en](https://ec.europa.eu/taxation_customs/business/vat/action-plan-vat_en)

## Digital tax administration overview

From a tax administration's perspective, there is a paradigm shift in the works. Where in the past Western European and North American tax administrations were considered to be the most advanced in the world, the digital best practices now come from Latin American and Asian countries. In Europe, especially Southern and Central European countries are digitalising rapidly, and Estonia is considered to be a frontrunner in digital authorities. The success stories coming from these countries are picked up rapidly by other countries and are accelerating the global trend towards tax digitalisation.

### The evolution of tax over the past 40 years



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## Digital reporting, analytics and exchanging information

Three disruptive trends in the global digitalisation of VAT are specifically worth addressing

1. Administrations moving towards digital reporting
2. Tax administrations building advanced analytical capabilities
3. Administrations sharing information to combat VAT carousel fraud



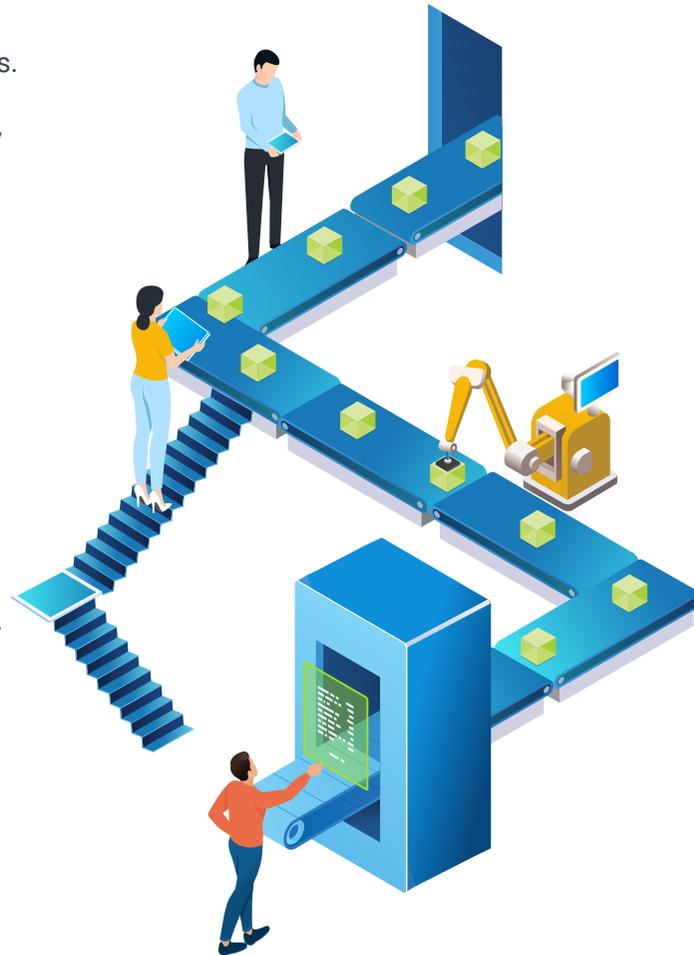
# 1. Administrations moving towards digital reporting

First, the way VAT is reported is being transformed. It was not that long ago that taxpayers were still required to periodically submit paper VAT returns to the tax authorities. Nowadays, **most tax administrations require taxpayers to submit the returns electronically (e-filing)**.

Furthermore, there is a clear trend that more countries are adopting (or looking at the possibility to adopt) mandatory e-invoicing processes in order to **gain full and real-time insight into the transactional (VAT) data of taxpayers**.

Having this real-time insight is an incredibly powerful tool to help tax administrations validate the VAT refunds granted to taxpayers. **Anomalies can be easily detected now that tax administrations have all the transactional invoice data in a standard format available in their system.**

This enables the tax administration to perform highly automated controls on the full population of invoices.



Italy is the latest addition to this list, with their introduction of the so-called SDI as mandatory for domestic transactions as per 1st of January 2019.

Another VAT reporting trend is the adoption of the Standard Audit File for Tax (**SAF-T**), or the equivalent of such an audit file. Where traditionally VAT returns consisted of aggregated data, **the SAF-T files provide tax administrations with structured, non-aggregated (i.e. on an invoice level basis) transactional data in a digital format.**

Poland will abolish the requirement to submit a regular VAT return and instead utilise its version of the SAF-T report (JPK\_VDEK) as a basis for calculating a taxpayer's VAT position. While in Poland the file must be submitted on a monthly basis, Spain has introduced the by now well-known SII, which requires taxpayers to provide non-aggregated reports of sales and purchase data in a standard format within four days of the invoice being issued or received and booked.

Thought leaders in the field of VAT believe that the 'end-state' of VAT reporting will be a 'pull' scenario<sup>5</sup>, where tax administrations will have a direct connection (e.g. through an API) with a taxpayer's system and calculate the VAT payable/receivable without direct involvement of the taxpayer.

*Although it will be a long journey towards such a system, the industry is clearly heading in this direction.*

<sup>5</sup> See for example figure 3 in Deloitte's report <https://www2.deloitte.com/insights/us/en/focus/cognitive-technologies/building-the-tax-function-of-tomorrow-today.html>



## 2. Tax administrations building advanced analytical capabilities

The next trend is related to the analytics capabilities currently being built by tax administrations. Not only are tax administrations collecting massive amounts of structured data through the e-invoicing and reports. It is not a question if, but when, such an international data standard will become a reality.

*Administrations are also developing Big Data capabilities that will turn these data lakes into valuable insights.*

Every 12-18 months, the OECD organises the Forum on Tax Administration (FTA) where tax administrations share experiences and learn from each other in this area<sup>6</sup>. This platform facilitates the ability for tax administrations to share best practices and leverage each other's success stories.



### 3. Administrations sharing information to combat VAT carousel fraud

This feeds into the final trend, also relating to the goals of the FTA meetings, which is the increasing exchange of information between tax administrations.

**One of the key challenges tax administrations are currently facing is the inability to benefit from the collected data beyond their country's borders.** The process of exchanging information is not yet mature enough to effectively combat cross-border fraud.

However, in the EU, the tax administrations are flexing their muscles by announcing the so-called Transaction Network Analysis (TNA) which will allow Member States to rapidly exchange and jointly process VAT data, leading to earlier detection of suspicious networks of VAT carousel fraud<sup>7</sup>. **This type of fraud represents about EUR 50 billion of the VAT Gap**, according to a study by the European Parliament<sup>8</sup>. The TNA is expected to close this gap significantly.

What if tax administrations can further develop these kinds of collaborative solutions? We might end up in a situation where every purchase transaction can be matched with the sales transaction at both ends by the respective tax administration. In combination with standardised invoices and data structures, this would provide the tax administrations with full insight into transactional data on a European or even global scale. **This would also imply that companies would need their data fully mirrored with their vendors and customers, as the tax administrations will be able to identify (and act upon) the slightest discrepancy in the data.**

On a side note, it is not completely unthinkable that such a global standard audit file will be achieved as the International Organisation for Standardisation (ISO) has been piloting a global audit data collection standard (including tax data) with 14 countries since 2015<sup>9</sup>.



**€50  
BILLION  
OF THE GAP IS VAT  
CAROUSEL FRAUD**

## The emergence of digital tax departments

What do all these changes and trends mean for companies and more specifically their tax departments?

**The good news is that the basic concept of VAT compliance will not change.** VAT data must be submitted on time, must be complete and accurate.

However, the digitalisation of VAT will change the meaning of these three elements significantly:

1. Timeliness
2. Completeness
3. Accuracy

### 1. Timeliness

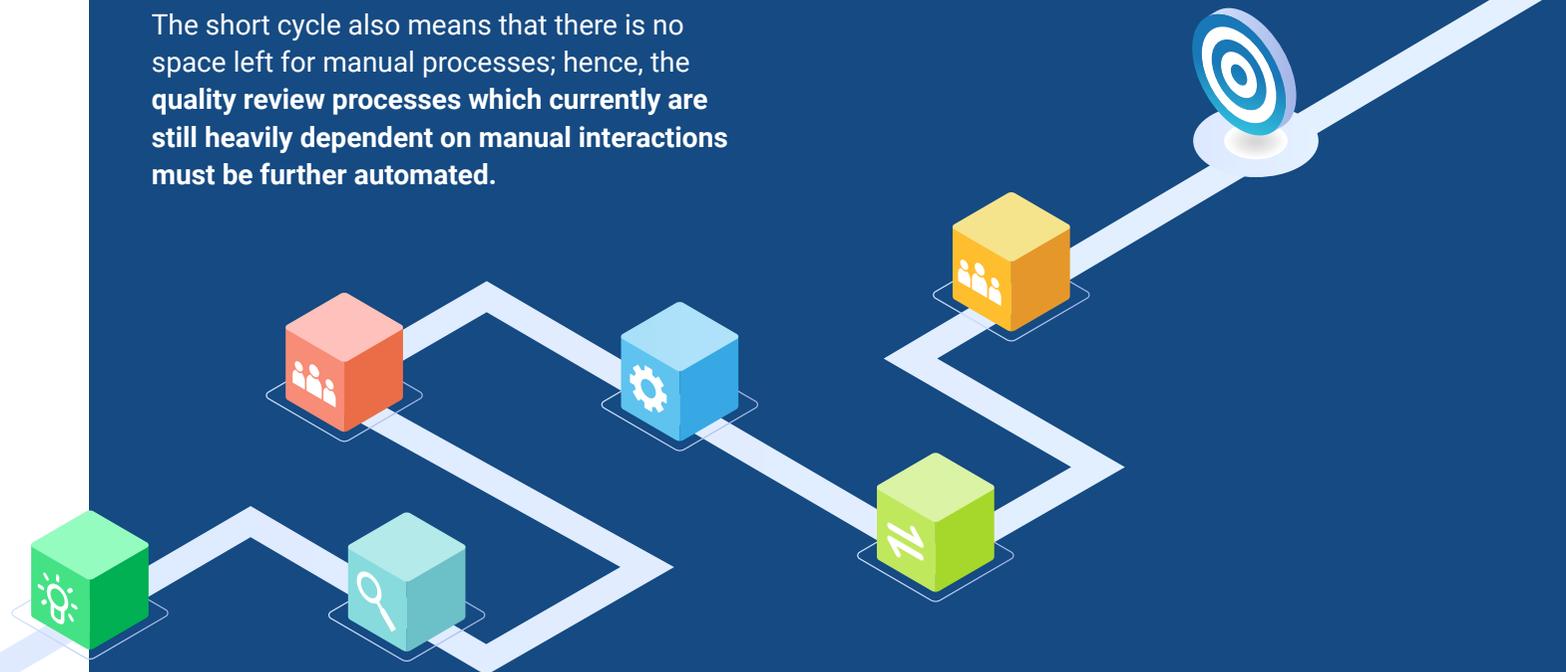
From a timeliness perspective, the impact is obvious. With the rise of real-time and near-time reporting (think of the four-day period allotted for a taxpayer to submit the Spanish SII reports), tax departments will be required to turn around the data faster than the traditional two to four weeks after the end of the tax period.

Tax departments will be unable to continue to embark on the traditional quality review cycle of data, as there is simply not enough time for the extended cycle.

The short cycle also means that there is no space left for manual processes; hence, the **quality review processes which currently are still heavily dependent on manual interactions must be further automated.**

As there are so many additional sources of data that will be required by tax administrations to be validated for the purpose of VAT compliance, **the VAT department will be closer to the business than ever before, and will have to take a more proactive role in managing VAT compliance at the source.**

The VAT manager may need to be involved in the process of master data management, automatic invoice processing, fully automatic intercompany settlements and a fully monitored supply chain to ensure all VAT relevant data is processed first-time-right.



## 2. Completeness

One of the challenges relating to the completeness of VAT reporting is connected to the standardisation of data files and the exchange of information between tax administrations as discussed before.

**In domestic situations, some tax administrations are already matching transactional data between vendors and their customers.** Again, the SII reporting in Spain, as well as the JPK filing in Poland are examples of where standardised and granular reports enable tax administrations to automatically match the data and identify the mismatches between the vendor's and customer's data.

It will only be a matter of time before tax administrations will have the capability to perform this matching on an international scale and far more easily identify mismatches between vendor and customer data.

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### 3. Accuracy

Within the end-to-end process – in order-to-cash, procure-to-pay and general accounting – the VAT accuracy of the data processed will remain one of the biggest challenges in VAT compliance, especially since the amount of data processed is growing exponentially.

**In only the last two years, 90% of the global data was generated<sup>10</sup>.** While the availability of data brings many solutions and opportunities, it also creates a challenge in itself. Will future VAT departments have a Data Architect on its team?<sup>11</sup>

In the current VAT landscape, tax engines and AP and AR specialists rule the VAT determination of transactions. The ‘automated’ VAT compliance checks during the VAT reporting process are mainly static, and data analytics is reactive and based on activities that occurred in the past.



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## Transactional data shifts driven by the digitalisation of VAT

### **The first shift is the accessibility of data.**

In the past, VAT managers were dependent on the VAT report (if any) extracted from the financial module of the ERP system after the Finance Department closed the books. The reports contained only the basic financial information about the transactions, often enriched with a tax code per transaction. Any other information about transactions had to be collected from other sources, either manually or via often complicated system integrations.

Over the last years, **companies developed tax data warehouses** in an attempt to solve this challenge. More data was collected from all kind of sources (for instance, supply chain + related information) and stored in central data repositories that could be accessed by tax departments for analysis and reporting purposes. However, the data available was dependent on the way the – often complicated and expensive – implementation of the tax data warehouse

*Consider the possibilities of having access to all corporate data for VAT analysis purposes at any point in time, even for the smallest company transactions. This development is exciting when it comes to the amount of data that will be made available to VAT departments.*

*This will definitely be the most exciting space to watch in the coming period.*

was performed. Furthermore, the data sitting in the warehouse did not always reflect the latest information (i.e. was not real-time) which still required warehouse transactions to be fixed even when they occurred long ago.

The future looks bright in this area, with the major **ERP players focusing on cloud-based solutions based on one big corporate data lake, which can be seamlessly integrated in real-time with all kinds of (tax related) applications.**

Another challenge lies in structuring and interpreting the data, in other words: building Big Data capabilities. This is the area where emerging technologies like artificial intelligence and machine learning will make the difference. Specifically in the area of semantical analysis (giving meaning to data), there is a lot to gain in the realm of VAT. This will definitely be the most exciting space to watch in the coming period.

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## The growing need for digital savvy tax professionals

With all the digital developments, tax departments must introduce new skillsets within their teams. Team members with different backgrounds should be onboarded and sitting resources should expand their knowledge and expertise in order to keep up with a rapidly changing world.

This includes education **on basic knowledge of technology, system architecture**, finance and business processes. This wide range of capabilities is key, as tax departments will need to understand processes to interpret data and determine the precise set of data to analyse.

**Mastering knowledge in these domains would result in VAT managers fully utilising the available data and making sense of the data lake in the most efficient and effective way possible.**

Equally important is the **training in soft skills**. VAT specialists will not be working in their own silo anymore, but will instead be collaborating much more with other departments and external stakeholders. Furthermore, in combination with the 'new style' Big Data analysis that will be performed by VAT departments, these resources should be qualified in communicating data insights, the so-called 'data storytelling.'



## The future tax professional



**On one side,** tax professionals will need a strong analytic skillset, technological savvy mindset and legal tax expertise.

**On the other side,** they will need to have data storytelling capabilities to communicate insights and the meaning of the data.

*Tax departments of tomorrow should embrace the right brain - left brain approach. This will help lead companies confidently and resolutely into the digital era.*

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## About the writer



Remco is VP Tax & Product Strategy at VATBox, responsible with his team to keep the VATBox systems fully up-to-date and design new features and solutions in the area of VAT, Benefits in Kind and Corporate Tax within the scope of the Travel Expense domain and part of the AP process. The mission is to develop those solutions that provide our clients more insight and control over their tax relevant data and increase the level of compliance, using VATBox patented AI.

Remco has a background in Indirect Tax legal advisory and leading inhouse indirect tax teams. He has a broad experience in Indirect Tax process optimization, automation and building Center of Excellence teams. He has been in different committees for EMEA and Swiss Indirect Tax associations. Remco is admitted to the Dutch bar of tax advisors.

**For more information on how to achieve the most out of your transactional data and make data-driven decisions**

Contact us

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## About VATBox

VATBox has successfully digitised the VAT/GST recovery workflow with its cloud-based enterprise recovery solution. Using intelligent automation, VATBox helps large corporations – including Fortune 500 companies – gain actionable insight into their transactional data, empowering finance and tax professionals with full data integrity, tight compliance and maximum savings. Fusing AI and Computer Vision with human expertise, VATBox provides a full spectrum of VAT/GST audit and recovery services. Benchmarks for tax, finance and procurement – aimed to encourage process improvements and compliance – are all collected in one easy-to-use portal with drill-down capabilities into every single transaction, no matter how small. Our expert team is just 'one-click' away, ready to help you start making data-driven decisions today.

Contact VATBox at [www.vatbox.com](http://www.vatbox.com)