

Integrating Oracle Solutions for High Performance Tax Audit Case Management

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EXECUTIVE OVERVIEW

The purpose of this white paper is to describe a high performance process model for tax audit case management and to define a solution architecture for this process. The paper also illustrates how the components of the solution can be integrated using Service Oriented Architecture (SOA) principles and practices to drive higher process efficiencies and recovery of money at risk. Finally, this paper shows how Oracle products fit within this architecture.

INTRODUCTION

The process of performing audit case management for tax is intended to ensure that all taxpayers are assessed and pay the correct amount of tax based on their specific situation.

The audit process is one of the most critical process performance areas in tax administration. A recent study by the Tax Policy Center confirms that the US IRS typically achieves a recovery of four dollars of revenue at risk for each dollar spent on additional audits¹. Therefore, process improvements for audit remain a key focus area in tax.

In many cases, tax audits are performed when there are issues related to taxpayer reporting or payment of tax obligations.

Tax audits can be resource intensive processes, and the information technology capabilities required to make audit case management effective can be fairly broad and sophisticated in scope.

This paper briefly describes the function and importance of tax audits, describes the basic set of information technology capabilities that are typically required to meet the business requirements associated with tax audits, and then presents a reference architecture for these IT capabilities. It then shows an example of populating the architecture with IT components that provide the requisite capabilities, using components drawn from a portfolio of Oracle infrastructure and

¹ Reducing the Tax Gap: The Illusion of Pain-Free Deficit Reduction, Toder, Tax Policy Center, 2007.

application solutions. Finally, it shows a sample-operating model based on the architecture, using those IT components.

WHAT IS A TAX AUDIT?

For many people the word “tax audit” brings a sense of fear and dread. The idea of a tax auditor poring through your financial records to uncover unreported income or over-claimed deductions or tax credits is not one that generally brings a great sense of joy.

Still, the functions of audit in tax are a critical part of a government’s ability to administer a fair and equitable taxation system. Good audit strategies and processes are used to educate taxpayers on their tax obligations, to uncover and treat cases of fraud and illegal tax evasion, to ensure proper reporting of taxable events and liabilities, and to generally promote maximum voluntary compliance to tax laws by the taxpayers in a given jurisdiction.

To perform a tax audit, a number of processes should be in place in a tax department.

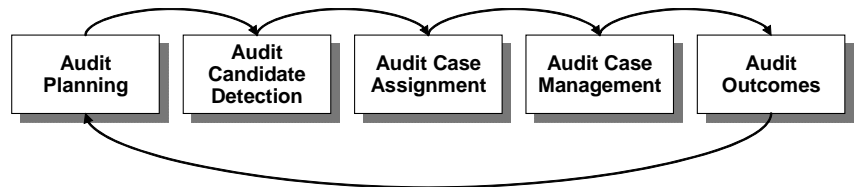


Figure 1 - High Level Tax Audit Case Management Process Flow

Figure 1 provides a high level view of the typical tax audit case management process cycle. The cycle of processes starts with a review of the strategy and plan for carrying out audit cases. In this part of the cycle, segment areas for audit focus are identified and the parameters that define the audit program for a tax agency are established. These parameters include the business performance measures that would be required to define the expected outcomes of the strategy.

Once the audit planning sub-process is complete, a tax agency will have the parameters that it needs to extract leads from the various data sources that it has at its disposal. This is the process of audit candidate detection. Various criteria are applied to these data sources in order to identify appropriate audit candidates that meet the profile established in the audit planning stage. Information leads are analyzed to pare down the candidate list to the list of audit cases that deserve the most attention.

The audit case assignment sub-process is responsible for assigning validated audit cases to the right resources that will carry out the audit. Case assignment rules can be very complex. The requirement here is to determine the correct assignment of cases and case tasks to the person or team or persons that have the skills and capacity to tackle them. The inventory of potential cases is constantly refreshed

and the case assignment process must work efficiently to ensure that case backlogs can be avoided.

The audit case management sub-process is composed of those tasks that an auditor or audit team carries out to pursue the audit and to reach a decision about the disposition of the case.

Finally, the dispositions of the audit cases are recorded and data related to the disposition is then fed back into the audit planning process for subsequent cycles. This feedback mechanism is a critical piece of an effective audit strategy, as results of current audit activities are used to inform the strategies and plans of the audit team.

WHAT ARE THE REQUIRED INFORMATION TECHNOLOGY CAPABILITIES TO ENABLE EFFICIENT TAX AUDIT?

Table 1 provides a list of the high-level business requirements associated with each of the audit stages described above. The table then defines the typical Information Technology capabilities that are associated with meeting these requirements.

Table 1 - List of High-Level Tax Audit Requirements and Associated IT Capabilities

Business Area: Audit Planning and Candidate Selection	
Business Requirements	IT Capabilities
<ul style="list-style-type: none"> • Match agency taxpayer data with reliable 3rd party data sources • Identify trends in taxpayer filing and payment behaviors • Search for patterns of under-reporting or non-filing • Search for patterns that indicate fraud, tax evasion and other potential of revenue at risk • Define audit campaign programs and objectives • Define audit selection criteria that produce the best predicted results of return 	<ul style="list-style-type: none"> • Data warehouse • Data analytics • Data mining • Predictive modeling • Define and track audit campaigns • Configurable business rules for audit case candidate selection • Execute case candidate selection rules automatically or interactively • Data and service integration with core tax processing systems

Requirements for Audit Planning and Selection

In the audit planning and selection stage, audit planners map out an audit strategy, identify segments of the taxpayer population that will be the focus of defined audit

campaigns, and identify and secure data sources for audit selection purposes. In addition to documenting the segments and targets for the defined strategy, this is the stage where data sources are identified and secured for audit selection purposes. Case leads are identified and evaluated using a number of analytical techniques including data matching, data mining, pattern development and statistical profiling.

Table 2 - - List of High-Level Tax Audit Requirements and Associated IT Capabilities (continued)

Business Area: Audit Case Assignment	
Business Requirements	IT Capabilities
<ul style="list-style-type: none"> • Assign cases and tasks according to classification of taxpayers (geographic, industry, size, risk profile) • Assign cases and tasks according to the skills and expertise of the tax agency audit personnel • Assign cases and tasks according to the existing workload distribution patterns and availability of personnel • Support audit case management for cases lasting months or years • Support audit case management for dynamic, and sometimes large teams 	<ul style="list-style-type: none"> • Configurable business rules for case assignment to individuals or groups • Executable rules for case assignment automatically or interactively • Automatic or manual escalation or re-assignment of cases or tasks

Requirements for Audit Case Assignment

In the audit case assignment stage, case leads and cases are assigned to tax agency personnel to be evaluated and worked. Case assignments are based on a number of criteria that define both the case to be assigned and the tax agency personnel that receives the assignments.

Table 3 - List of High-Level Tax Audit Requirements and Associated IT Capabilities (continued)

Business Area: Audit Case Management	
Business Requirements	IT Capabilities
<ul style="list-style-type: none"> • Attach work papers and documents to one or more cases • Record time and expenses spent by auditors and audit teams on each case • Associate cases to one another based on user-defined criteria • Support for definition of tasks to be performed, and the order and scheduling of tasks, including human based tasks such as taxpayer meetings, phone calls, etc. • Support automated case tasks, including automatic and ad-hoc generation of notices and correspondence • Support various modes of case work, including desk audits, team audits and field audits with disconnected, laptop-based audit teams • Support taxpayer interaction via phone or Internet 	<ul style="list-style-type: none"> • Integrated document and case management • Time and expense recording linked to case work • Case lifecycle definition and execution • Dynamic assignment of activity plan to case based on user-defined criteria • Integrated case and correspondence management and notification generation • Field audit and disconnected user support • Taxpayer service via phone and Internet • Services to calculated tax, penalty, interest and fees based on different audit outcome scenarios

Requirements for Audit Case Management

It is in the audit case management stage that case activities are carried out and documented. Requirements include the ability to work with case files in both desk and field audit scenarios, to assign activity treatment streams based on the characteristics and risk profile of the case at hand, and to provide audit case workers with the tools they need to complete and close their cases.

Table 4 - List of High-Level Tax Audit Requirements and Associated IT Capabilities (continued)

Business Area: Audit Outcomes	
Business Requirements	IT Capabilities
<ul style="list-style-type: none"> Record case outcomes and results Associate case outcomes with defined audit campaign that the case is a part of Report on aggregate outcomes based on campaign association and other criteria (timing, geographic, industry, etc) Update taxpayer risk profile based on outcomes of audit case 	<ul style="list-style-type: none"> Formalized case closure and capture of case statistics Aggregation of case results, including association with audit campaign Taxpayer risk profile services Support for static and ad-hoc reporting of case results Association of case results with defined business process management goals and metrics defined during the audit planning stage

Requirements for Audit Outcomes

In the audit outcomes stage, the outcomes of individual audits are recorded and evaluated. Metrics on the performance of each audit activity are captured and the disposition of each case is recorded.

A REFERENCE ARCHITECTURE FOR TAX AUDIT

Based on the outline of business requirements and associated IT capabilities, a reference architecture can be defined. The reference architecture model for tax audit is illustrated in Figure 2.

Each of the boxes in the diagram represents layers of IT functionality that support the requirements defined in our tax audit requirements list. The IT capabilities and functions required to meet the business requirements for tax audit are provided by technologies in each category.

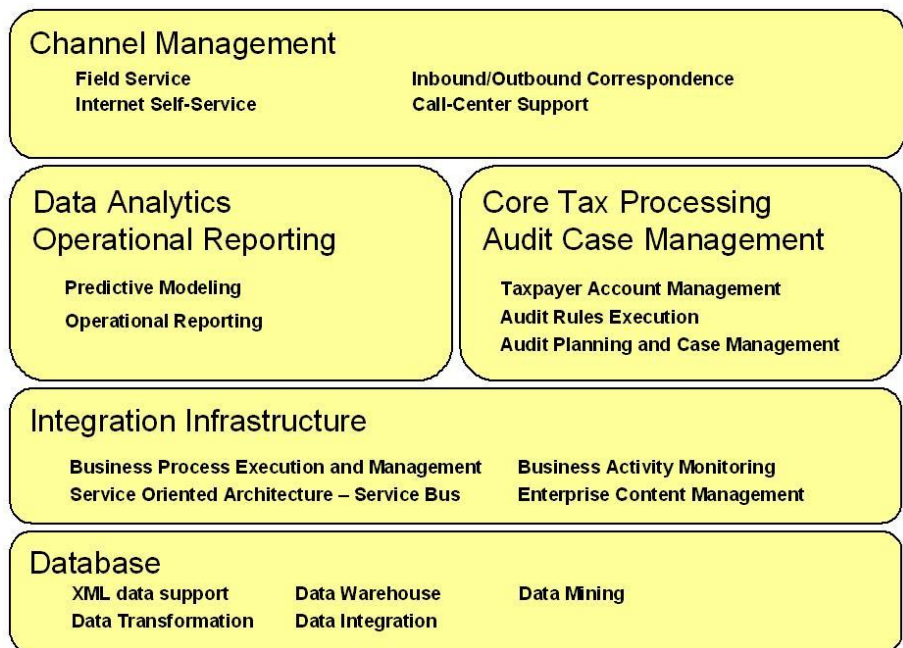


Figure 2 - Reference Architecture for Tax Audit Case Management

The reference architecture starts with the database layer. This is the layer where the capabilities to build and exploit tax audit data warehouses exist. The audit data warehouse is typically composed from a number of sources, including the core tax processing system in the tax agency (e.g. Oracle Enterprise Taxation Management), and any number of internal and external data sources of interest.

The next layer, integration infrastructure, includes capabilities to model and monitor integrated business process flows related to tax audit case management – for example the process for creating and closing audit cases. This layer also includes the base infrastructure for enabling application systems to collaborate with one another using industry standard SOA principles and standards. The integration layer also includes other core infrastructure capabilities such as enterprise content management for handling the variable document management needs across audit operations.

The core tax processing and audit case management layer is where the core business applications reside and operate. These are the systems that manage taxpayer accounts, return and payment processing, initial audit case lead detection, and the case management capabilities themselves.

The data analytics and operational reporting layer represents the IT capabilities to build analytical reports throughout the performance of the tax audit case management business area. It also contains various analytical tools used to provide real-time decisions and rules for assignment of activity plans (treatment streams) based on the risk profile of the taxpayer under consideration.

Finally the channel management layer contains the capabilities that facilitate multi-channel communications with taxpayers and other parties for the purpose of completing cases. This layer contains capabilities to support taxpayer correspondence, call center interactions and web self-service for taxpayers under audit.

Figure 3 illustrates what this architecture would look like when populated with solutions from Oracle.

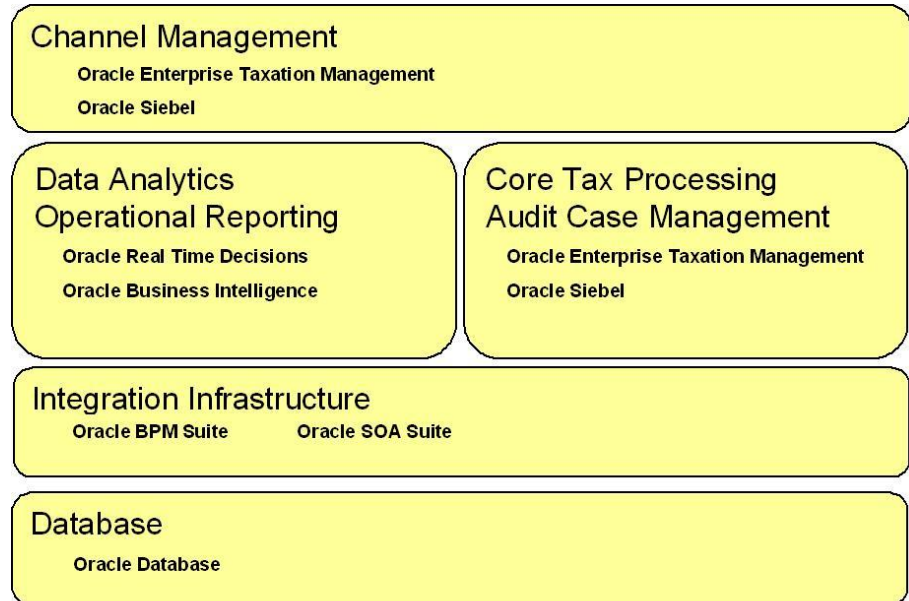


Figure 3 - Reference Architecture for Tax Audit Case Management with Oracle Solutions

An Operating Model for Tax Audit Case Management

The operating model illustrates a typical process and data flow scenario for tax audit management. Figure 4 provides a sample operating model view for tax audit based on the reference architecture defined above.

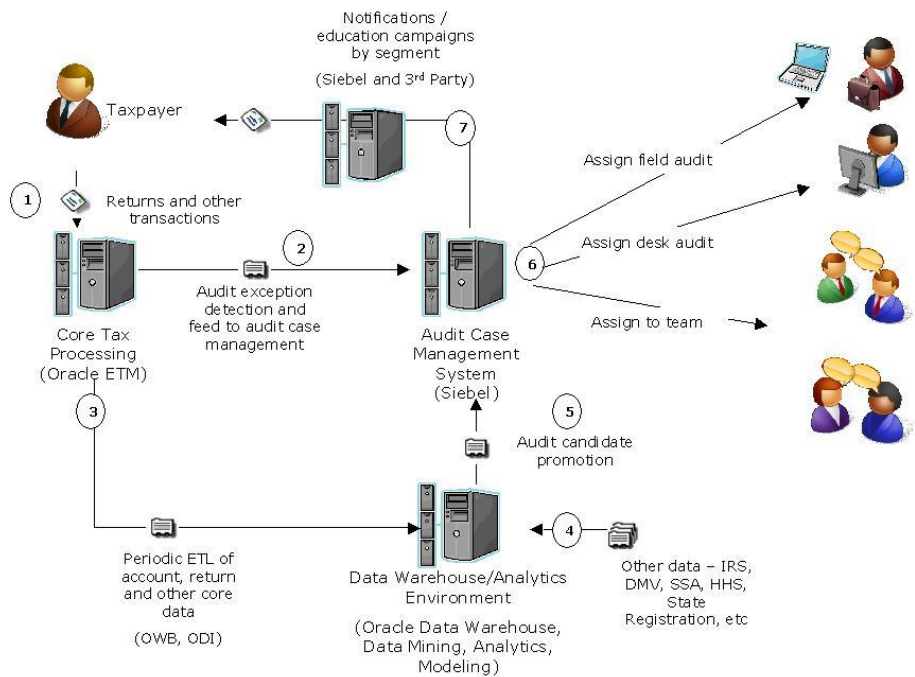


Figure 4 - Concept of Operations for Tax Audit Case Management with Oracle Solutions

The operating model is interpreted by following the labeled numbers in the illustration.

In step 1, a taxpayer supplies tax returns, tax payments and other transactions to the tax department where they are processed through a core tax processing system. For example, the Oracle Enterprise Taxation Management (ETM) system is responsible for processing these incoming taxpayer transactions and maintaining the authoritative taxpayer account management data.

In step 2, business rules for identifying high-risk transactions are executed in Oracle Enterprise Taxation Management (ETM) and these transactions can be immediately forwarded to the Audit Case Management System, which is allocated to Oracle’s Siebel solution.

As an alternative to this immediate detection and routing of cases to Siebel, step 3 illustrates a more generic extraction of core taxpayer data and the extract, transform and load (ETL) of this information into a data warehousing environment on a periodic basis.

Step 4 illustrates the common practice of merging and comparing core tax administration data with data from other government agencies and contracted third party data providers. The use of these data sources is critical for the data mining and analytics that are used to detect audit candidates that meet the selection criteria laid out during the audit planning stages.

Step 5 illustrates the promotion of the audit candidates from the data warehouse environment into the tax audit case management solution, provided by Oracle's Siebel solution.

In step 6, automated workflow processes in Siebel determine the correct case assignment and activity plan (or "treatment stream") for each incoming case lead. The case leads are assigned to different individuals and teams according to the characteristics of the case and to the properties of the tax audit workforce in the tax agency.

Finally, in step 7, the tax department initiates communication with the taxpayers about the audit case lead, which closes the process loop for the operating model. In the illustration, Oracle's Siebel solution is used to generate notifications and correspondence to the taxpayer, which is typically fulfilled and delivered using third party solutions in the industry.

The presence of the Oracle SOA and BPM Suites in the operating model conveys the concept that the entire set of processes captured in the model can be managed, monitored and facilitated through base infrastructure capabilities around web services and integrated business process management.

Summary

Tax audits are an essential core competency for tax administrations around the world. The extended set of business processes that realize an agency's audit strategies are dependent on the availability of a range of IT capabilities.

In this paper we have defined a generic tax audit planning and execution process, and described a reference architecture for that process. We have shown how that reference architecture could be populated with Oracle solutions, and we have sketched a sample-operating model based on the architecture with those solutions.



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Oracle Corporation
World Headquarters
500 Oracle Parkway
Redwood Shores, CA 94065
U.S.A.

Worldwide Inquiries:
Phone: +1.650.506.7000
Fax: +1.650.506.7200
oracle.com

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