

Tax Integration

How to complete the M&A integration process, minimize disruptions, and achieve desired synergies.*

Amid the excitement of a transaction, the tax aspects of integration are often viewed as overly complex and “back-burnered” to the realm of post-deal business integration timelines. This often proves to be a costly mistake, as tax considerations are the drivers that shape legal entity integration, transfer pricing and operating model rationalization, and employee deployment. While tax integration may be admittedly challenging, careful planning before and immediately following transaction close can have a significant impact on the combined company’s future effective tax rate, cost of tax compliance, and ability to utilize tax attributes.

Although the tax positions of a target company are carefully studied as part of the due diligence process, acquiring companies often fail to pay enough attention to the intricate requirements of integrating the operational aspects of the tax structure and tax department function to enable a smooth transition.

The early involvement of the tax department in integration decisions is critical because it enables the company to achieve desired pre-acquisition structuring while coordinating with other functional teams such as legal, finance, IT, and HR to prepare a plan for Day One and post-acquisition activities.

The Issues Our Clients Face, The Actions We Help Them Take

At PwC, we understand the importance of getting the fundamentals of integration in place as quickly as possible during a deal to minimize disruptions and achieve synergies. We support our clients by rapidly launching integration efforts to Set the Course, Plan for and Execute Day One, and Design and Maximize Future State Operations. This is the approach PwC delivers in managing the integration as an enterprise-wide business process.

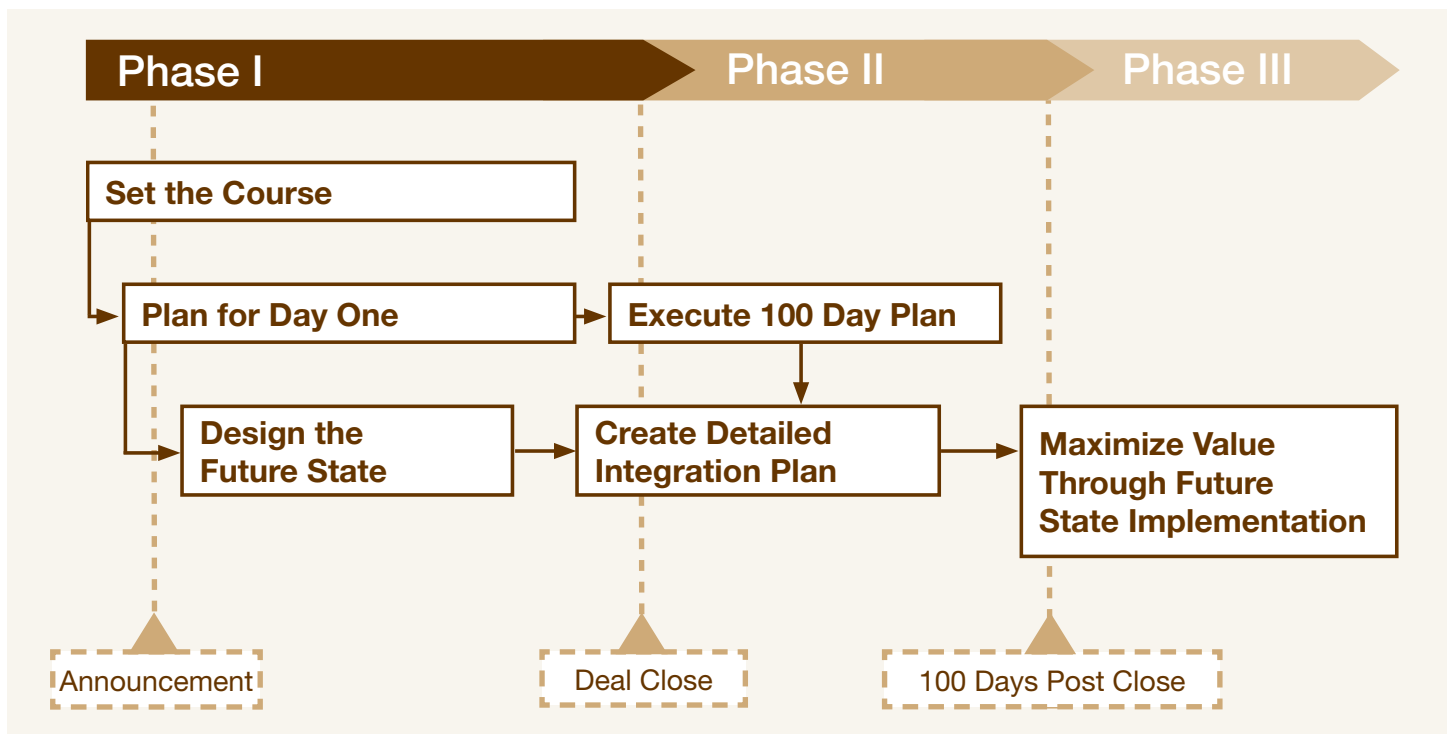


Figure 1—The PwC integration process follows a sequence of coordinated steps to focus resources and capital on the right things at the right times.

Set The Course

A merger or acquisition, like other large scale corporate change, is an excellent opportunity to set a new course, both operationally and across the various support functions of the newly combined business. Across all functions, setting the course involves establishing clear leadership and role clarity during the transition. This empowers members of the integration team—including tax—to communicate effectively and take decisive action.

Setting the course for tax success requires a disciplined focus on key value drivers:

- Creating a tax efficient structure that produces an optimized effective tax rate and allows for efficient cash movement and repatriation
- Rationalizing the overall legal entity structure to minimize compliance and administrative costs while preserving potential tax attributes
- Designing a reporting system that will allow for efficient tax accounting and compliance.

Early stage cross-functional communication is critical to successful tax integration since tax planning can be significantly impacted by legal, finance, IT, HR and other decisions. For example, the decision to change a legal entity's structure or historical operations, adopt new general ledger systems, relocate material functions, or terminate employees can all have a significant impact on the combined company's tax position and ability to comply with tax accounting and tax return deadlines.

Leading practice is to identify a tax integration lead—a person who is responsible for identifying sub-teams and leaders for each tax area of interest. The tax integration lead is primarily responsible for ensuring that tax matters are addressed by other functions and tax-related input is considered within other major workstreams, leading to seamless integration planning.

Plan For and Execute Day One

Even if the best decisions are made as you Set the Course, much can go wrong upon close absent proper planning and execution. While Day One is a milestone for celebration, it is also the time for smooth transition of mission critical operations.

The goal for Day One is to have a plan in place to manage the combined company's tax function and meet the financial and compliance reporting obligations of the collective organization over the next nine to 12 months. Ideally, while setting the course, critical decisions have been made jointly with cross functional teams and now it is time to execute the plan.

While setting the course, many companies decide that duplicative legal entities within a jurisdiction will be eliminated post close in an effort to reduce complexity and the cost of compliance (both for tax return and statutory account purposes). However, the need to reduce complexity must be balanced against whether there are any valuable tax attributes—such as tax losses, credit carryforwards, or high tax basis—which may be inadvertently eliminated in the absence of careful structuring.

For example, in some jurisdictions, a merger of a legal entity with tax loss carryforwards may prohibit the use of the tax losses. In other jurisdictions, the ability to preserve tax losses depends on whether the buyer or target's legal entity survives the merger. It will be critical for the tax integration team to be involved in the decision about how best to eliminate legal entities.

Tax due diligence procedures may have been undertaken while setting the course to identify potential historic tax liabilities inherited in the transaction. It is critical that tax exposures identified during due diligence are further researched, properly documented, and recorded in purchase accounting. Note that under FAS 141R, liabilities not identified in purchase accounting (generally within one year of the close of the acquisition) and not accrued as part of purchase accounting will result in an adjustment directly to the provision for income taxes in the period incurred.

The acquiring company can anticipate people attrition in the acquired company's tax and finance department. Identifying and securing tax related documentation of the acquired company is critical to ensure the combined entity will be able to comply with its tax accounting and tax compliance deadlines. Additionally, the acquiring company may be required to defend the historic tax positions taken by the acquired company under examination long after the acquired company's personnel have left the company.

Some Things to Remember When Integrating Tax Functions

- **Understand what's in and what's out.** It is critical to identify which tasks are owned by the tax function. Areas such as Section 280G (i.e. golden parachute provisions) and Section 409A (i.e. deferred compensation) are often handled by HR or Legal, and cash repatriation is often handled by Treasury.
- **Proactively manage cross-functional dependencies between Tax and other back-office functions, including Legal, Finance, IT, and HR.** The decisions made by other functional areas may have an adverse impact on the combined company's tax position without proper tax input. Be sure there is a clear process for identifying and escalating tax review of cross-enterprise integration activities.
- **Work with advisors that have appropriate global reach.** The more globally dispersed your operations, the more you will need to depend on local legal and tax advisors to deliver on plans that are carefully tailored to the local taxation system complexities.
- **Develop an integration schedule that meets the ongoing financial reporting and compliance obligations.** Quarterly tax accounting and tax return deadlines will still need to be met while the integration process is underway. Be sure that accounting and tax information required to meet these deadlines continues to be accessible during the integration process. Additionally, the complexity of reporting for the combined operations must be considered.
- **Design a tax organization structure with an optimal number of people with the right skills in the right positions to support the integration.** The integration process and resulting tax structure may require tax personnel to transition to new roles, or may require the hiring of personnel with the optimal skill sets to support the new organization.

Design and Maximize Future State Operations

A critical post Day One tax integration activity is to develop a strategic plan for the combined function. The goal is not simply to select leadership, reduce headcount and assure continued operations, but to improve all tax-related activities—positioning the new department to be effective in the future. The integration strategy should be aimed at establishing proper controls, increasing efficiency, and reducing risk.

At a minimum, tax integration planning should address the following:

Tax Department Function

- Build a department with appropriate skills and capacity for the work
- Improve the quality of the tax deliverables
- Strengthen internal controls
- Connect tax personnel globally

Tax Compliance

- Review filing requirements for the combined company
- Ensure IP platforms are equipped for additional compliance burdens
- Identify jurisdictions where filing combined or stand-alone tax returns

Purchase Accounting

- Evaluate IP ownership to ensure appropriate deferred tax accounting
- Assess stock option plan assumptions and ensure appropriate deferred tax and goodwill accounting are applied
- Ensure potential tax exposures are properly identified and recorded, where appropriate
- Establish appropriate APB 23 assertions (cash permanently invested off-shore)
- Assess the need to record or release a valuation allowance on acquired tax attributes

Tax Impact of Operations

- Identify location of IP ownership and consider IP ownership strategies
- Develop tax efficient value chain (e.g., consider US versus foreign sourcing of income, location and profitability of manufacturing operations, use of principal distribution companies, etc.)

Legal Entity Rationalization

- Review combined legal entities by jurisdiction
- Develop entity consolidation plan, identify tax considerations and timing of steps
- Determine the cross-functional requirements, such as legal input and foreign jurisdiction assistance
- Identify local country filings and other requirements

Offshore Cash

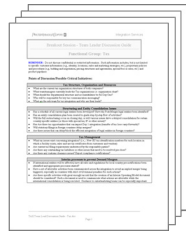
- Consider global treasury strategies such as the use of internal leverage, intermediate holding companies, financing entities, and cash repatriation plans
- Identify whether off-shore cash can be repatriated and at what cost

Our Approach for Delivering Tax Integration Success

Our disciplined approach to tax function integration helps companies achieve early wins, build momentum and instill confidence among stakeholders. We take an active, hands-on approach to helping clients focus on the right things at the right times, creating early and sustainable capture of deal value. We deliver time-tested integration processes to support client integration teams and supplement those teams with experienced resources to fill technical and resource gaps as required. We customize our tools and services to complement each client's specific needs and internal capabilities.

Our Tools for Tax Integration

Team Lead Discussion Guide
Guide for functional team leader with questions that trigger thought to assist in rapidly defining integration scope

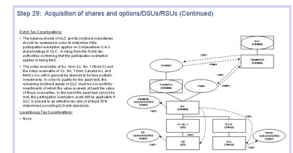


Legal Entity Matrix
Model matrix used to identify important tax attributes to be considered in Tax Steps Plan

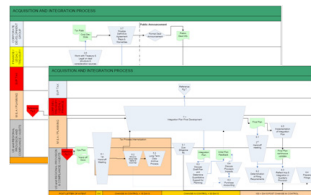
Entity	Country	Legal Form	Ownership				Control				Tax Residency	Tax Status	Tax Treatment		
			Parent	Subsidiary	Partner	Shareholder	Parent	Subsidiary	Partner	Shareholder					
USA	USA	C-Corp													
UK	UK	Private Ltd													
FR	FR	SAS													
DE	DE	AG													
IT	IT	SpA													
ES	ES	Sociedad Anónima													
Spain	Spain	Sociedad Anónima													

Tax Integration Workplan
Model integration workplan used as a "starter" set of tasks to jump start the functional workplan development effort

Tax Steps Plan
Model plan for documenting tax steps to be followed in Legal Entity Consolidation Plan



Integration Process Flowchart
Model flowchart depicting how the tax function process integrates with other functions



Legal Entity Consolidation Plan
Model plan and guidance for coordinating cross-functional and cross-border timelines and responsibilities to drive early legal entity integration for effective synergy realization

Entity	Transaction	Transaction Type	Legal Form	Country	Legal Form	Country	Legal Form	Country	Legal Form	Country	Legal Form	Country	Legal Form	Country	Legal Form	Country
USA	Acquisition	Share	C-Corp	USA	C-Corp	USA	C-Corp	USA	C-Corp	USA	C-Corp	USA	C-Corp	USA	C-Corp	USA
UK	Acquisition	Share	Private Ltd	UK	Private Ltd	UK	Private Ltd	UK	Private Ltd	UK	Private Ltd	UK	Private Ltd	UK	Private Ltd	UK
FR	Acquisition	Share	SAS	FR	SAS	FR	SAS	FR	SAS	FR	SAS	FR	SAS	FR	SAS	FR
DE	Acquisition	Share	AG	DE	AG	DE	AG	DE	AG	DE	AG	DE	AG	DE	AG	DE
IT	Acquisition	Share	SpA	IT	SpA	IT	SpA	IT	SpA	IT	SpA	IT	SpA	IT	SpA	IT
ES	Acquisition	Share	Sociedad Anónima	ES	Sociedad Anónima	ES	Sociedad Anónima	ES	Sociedad Anónima	ES	Sociedad Anónima	ES	Sociedad Anónima	ES	Sociedad Anónima	ES
Spain	Acquisition	Share	Sociedad Anónima	Spain	Sociedad Anónima	Spain	Sociedad Anónima	Spain	Sociedad Anónima	Spain	Sociedad Anónima	Spain	Sociedad Anónima	Spain	Sociedad Anónima	Spain

Critical Dependencies
Example dependencies to assist in accelerating the business requirements identification from other functions

Function	Dependency	Priority	Status	Owner	Start Date	End Date
Legal Entity	Identify all legal entities	High	Complete	Legal	2023-01-01	2023-01-15
Ownership	Identify all ownership structures	High	In Progress	Legal	2023-01-15	2023-02-15
Control	Identify all control structures	High	Not Started	Legal	2023-02-15	2023-03-15
Tax Residency	Identify all tax residency structures	High	Not Started	Legal	2023-03-15	2023-04-15
Tax Status	Identify all tax status structures	High	Not Started	Legal	2023-04-15	2023-05-15
Tax Treatment	Identify all tax treatment structures	High	Not Started	Legal	2023-05-15	2023-06-15

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