eBiz Answers

WHITEPAPER:

Oracle R12 – One or multiple Operating Units?

The intention of this document is to provide information to help you decide whether you should look at using multiple operating units or one operating unit with multiple legal entities.

CONTENTS:

Introduction:

The challenged faced by any company implementing a new ERP solution, whether a single entity or a global conglomerate, is to capture the complex business requirements yet to keep the structure as simple as possible. Creating a highly complex organisation structure is likely to lead to greater data processing needs as well as a more labour intensive maintenance requirements but creating a risk that the solution initially designed to help the company, ultimately leads to issues that end up consuming more resource.

Any solution architect will be considering this when they design the organisation structure deciding the best approach for the number of ledgers, what legal entities will use these ledgers and how many operating units will be needed to capture the data from the sub ledgers such as the Payables or Receivable modules.

The 11i approach was often to keep things as simple as possible, with one ledger where possible and only one operating unit linked to this ledger. The primary driving factor was the time it would take to run reports, opening and closing the month and entering data across the different legal entities. Each additional Operating unit meant that a new responsibility was required and this meant that a user would have to switch between these responsibilities each time they wanted to enter any data or do any month end processes for example. If you had 10 legal entities, this meant that the same task, if 10 operating units were used, one for each Legal entity, would have to be repeated each time. This of course would take a huge amount of time compared to one operating unit that all 10 legal entities were assigned to!

Oracles' 'Release 12' solution change the playing field and ultimately the way the organisations could be established. First, ledger sets allowed multiple ledgers to be linked together as a ledger set providing that the same calendar and chart of accounts was used. A ledger set could then be assigned to a responsibility effectively giving access to the data in all of those ledger contained in the ledger set! Second, and more importantly, the ability to create security profiles meant that access to operating units and inventory orgs could now be combined together. This means that those 10 legal entities could now have 10 operating units per legal entity and added to one or multiple security profiles. A security profile and not an individual operating unit could now be assigned to a responsibility, giving it access across all 10 operating units! So now the ability to maintain simplicity with one responsibility to enter data and process month end is achieved but with the added benefits of the diversification that multiple operating units can bring.

This document is intended to highlight the potential issues if the correct number of operating units are not used.

Recommended Approach:

The minimal number of operating units needed should at least be one per country per legal entity. This means that if a legal entity is established in France and only operates in France then only one Operating unit is needed. If however a similar French legal entity is registered and located in France but also has legal branches (or permanent establishments) in Germany and Italy, then 3 operating units would be the preferred route, one for each of the countries that the legal entity is registered in.

I would also apply this rule if a company had 5 legal entities in France, meaning that 5 operating units would be created, one per legal entity because each legal entity only has one country.

Difficulties Faced:

So, if a company for example decided to create one EUR ledger for Europe and only one operating unit for Europe instead of following the rule in the recommended approach, below would be some of the difficulties faced that may or may not lead to serious issues further down the path of the implementation project.

Default Data

With each operating unit, it is possible to set defaults which are used when transactions are entered, suppliers or customers created or setup done. The default currency for invoices being entered can be based on the operating unit, as is the accounting, such as the liability account or receivables accounts. With only one Operating unit, only one default can be used and as such either manual intervention is needed to change the value or custom code or SLA to ensure the correct account code combination is sent to the GL.

Which Legal Entity?

If you create the legal entities in Oracle under the Legal Entity Manager Responsibility, there is a high chance that you have legal entities that are used as holding companies, are dormant or having a naming convention which means the different companies are very similar in name. If you need to get users to choose the correct legal entity, the values that they can choose from may be confusing and present a risk in getting the wrong one. With an operating unit, you will only set up the operating unit that you need and will then link the legal entity to it. So the users only need to worry about the operating unit they are in with the legal entity automatically assigned.

Party Data

Suppliers and customers when set up assign the sites to operating units. If only one operating unit is used then it is possible for the wrong supplier site to be chosen when an invoice is being entered. This would then lead to incorrect accounting hitting the GL which may not ever be discovered. Multiple Operating units limit the user to select only the sites that are linked to the operating unit that they are working with.

Purchasing

In a scenario where you have one Operating unit with Legal Entities/Balancing Segments and appended to the operating unit you also have Inventory Organizations representing the different locations. When a purchase order is raised for one entity, the expense account gets defaulted with the expense account as defined for the Ship to Organizations hence the correct code combination. The other side of the entry, the Expense AP Accrual account is where the problem lies as this is set at Operating Unit level hence if the balance segment value of the entity for the expense is different to that of the Expense AP Accrual, a problem arises. This is one of the drawbacks of using one Operating Unit. Of course, SLA can be used to derive the correct balancing segment on the expense AP accrual but when we are looking at it from a Global Perspective, it doesn't make sense as you end up with a multitude of SLA rules for something that could easily have been resolved.

Purchase Orders

Purchase orders are set up and only linked to an Operating Unit, there is nowhere to link the Legal Entity to the purchase order! So the buying team can make purchases knowing who the legal entity they are buying for but this information is not available to the Payables team via the matched transaction and the payables team could be in a different country on a different time zone. The point of making a purchase order is to capture all the information up front to save time downstream, but as you cannot assign the Legal Entity to the purchase order then this information will be needed at a later date slowing down the process.

Purchase Order Matching

If purchase orders are used then when matched, the purchase order will automatically select the correct operating unit without the user having to first choose the operating unit.

Month End Closing

It is often thought that having one operating unit assigned to multiple legal entities would make the month end close easier as all the month end steps can be applied at once. A responsibility that has a security profile assigned to it containing multiple operating units can perform the same month end tasks across all operating units at the same time[1] making the close time the same as if only having one operating unit. However, as an added feature, if one there was an issue in closing one of the legal entities and multiple operating units were used, then it would be possible to close the other operating units to allow business as usual rather than having to delay the period close whilst the problems were resolved with the legal entity with the issue.

Printed Documents

Particularly in Europe, the printed documents that are sent out to customers such as statements or invoices need to comply with local statutory requirements. If only one operating unit is used then it is far harder to differentiate as to what data to put on to those printed documents. However, multiple operating units will allow for formatting, language and other statutory requirements per operating unit.

Payables Options by Operating Unit

Exclude Tax from Discount Calculation is only set once so if there is a legal requirement to not discount the tax then this would be difficult without this option which is set at Operating Unit level.

Country Localisations

Whilst Oracle has been designed to work in every country globally, the out of the box solution cannot meet every single statutory requirement for every country. For this reason, Oracle provides country specific localisations which when assigned, need to be differentiated from the 'common' solution. In order to do this, the localisations need to be assigned to specific responsibilities and often require a separate operating unit where custom code is needed. Utilising one operating unit for multiple legal entities that span multiple countries could cause issues that would need custom code to resolve.

Transaction Types

If only one operating unit is used then all the transactions types needed will be visible when being chosen potentially making it harder for a user to choose the correct value and risk making a mistake, choosing the wrong transaction type and generating a transaction for one legal entity that should have been for another. Multiple operating units would allow the transaction types, receipt classes, sources etc. to be linked and limited by the operating unit making it easier for users to choose the correct values to use.

Transaction Tax

Without doubt, one of the most import things to get right on any implementation is the transactions taxes being calculated and ultimately reported. Whether Sales and Use tax, VAT or GST, if taxation is not right then a company could be subject to huge fines and time consuming tax audits. The emphasis to get the tax solution correct is paramount for the success of any ERP implementation and the number of operating units

---

[1] Some custom processes maybe required.

can heavily influence the creation of the tax solution. Having multiple operating units, at least by country allows the tax to be easily controlled and confined to just that one country's tax regime[2].

Tax Receivables 'Bill From' Address

The Bill from address for AR transactions comes from the address that is linked to the legal entity unit. This means that if only one operating unit is used then you will need to rely on transaction types that can be linked to a legal entity to help create the correct invoices. But if more than one Legal Entity are linked to the Operating Unit then you will need some way to automate the process which would otherwise be automated if linked to the OU.

Tax Payables 'Bill To' Address

The Bill to address for AP invoices comes from the address that is linked to the Legal Entity. This means that you need to choose the legal entity manually each time you enter a transaction and because a purchase order is only linked to an Operating Unit and not the LE, it means that no Legal Entity is defaulted in when the AP invoice is just linked to the matched to the invoice. Take for example an Operating Unit with 50 legal entities assigned to it. All the Purchase orders are linked to the Operating Unit but for each invoice entered, the user not only has to choose the correct legal entity but they will also need to work out which one to use which is a risk in itself. As all the tax information is linked to the Legal Entity such as the registration details, party classifications etc., if you don't choose the legal entity then all transactions just go to one! This can cause issues with tax setup and intercompany processes where the tax exemptions are driven by the use of the same VAT group number or certain tax regimes and rules are linked to just the legal entity, all this is lost.

Tax Accounts

When a tax rate is created, it needs at least one tax account assigned to it which is done by linking the account to a ledger and an operating unit. For each operating unit that may use that particular tax rate, a tax account needs to be assigned to the rate. This means that a default tax account will be used for each operating unit. If only one operating unit is used that is linked to multiple legal entities (and we assume that each legal entity has its own balancing segment) then only one tax account can be assign to that rate. Customisation, usually by using SLA will then be needed in order to correctly determine what account to use and push to the GL. The issue with the SLA option is that the change to accounting takes place after the distribution lines have been created so the distribution lines will show one GL code but what actually hits your GL is a different GL code. This of course can be avoided if an operating unit is used for each Legal entity per country.

Tax place of supply

For a tax regime to be selected to be used, it needs to match the country of the tax regime against the value determined by the place of supply rule linked to that regimes tax rules. The 'place of supply rule' will determine the country used in the 'ship to, the 'ship form', the 'bill from or 'bill to' and if this matches the tax regime country then the tax will be activated. As an example, if only one operating unit is used for a European rollout where the Finnish site (who is registered for VAT) sells a product to Sweden and ships from a distribution centre in the Netherlands then it is possible that the single Operating unit (the bill from) is defaulted to be in the Netherlands, the Ship from is also in the Netherlands and the Bill To and Ship To are Sweden, then at no state can the place of supply rule determine Finland unless the legal entity is changed and therefore not activate the Finnish VAT.

---

[2] As described in this document, tax regimes can be assigned to a legal entity but this then requires the manual selection of that legal entity each time.

Tax Rules

Each tax regime needs to be assigned to the operating unit or legal entity that may use them. If only one tax regime is assigned to an operating unit then only that tax regime will ever be called upon. If an operating unit is used for multiple country tax registrations then each of those tax regimes are assigned to the operating unit. The more tax regimes assigned to an operating unit, the more complex the tax rules need to be in order to correctly determine the tax to be used as it is possible for multiple taxes to be determined for each transaction. With one tax regime per operating unit, the rules can be simplified as there is no possibility of the wrong tax regime calculating a tax for the transaction. The Tax regimes can also be linked to the Legal Entity within the Operating unit but this can have additional problems as indicated in the next paragraph.

Choosing the Legal Entity

It is possible to link tax codes to the legal entity but the biggest drawback to this is that during invoice entry in payables, a Legal Entity must be chosen each time. For manually entered transactions this may seem an acceptable option but it is difficult for users to know which operating unit to choose and can easily take the wrong Legal Entity by mistake and because they are of the same Operating Unit as the other Legal Entities, there are no restrictions on access to suppliers as we would see when separating by Operating Unit. With the separate operating unit, if you put the wrong Operating unit in then try and chose the supplier, it won't exist! And because the purchase order is not linked to any Legal Entity then one of the advantages of using purchase orders is lost as invoices must first choose the Legal Entity 'Customer Tax Payer ID' on the invoice workbench before choosing the PO number.

Same VAT Group

The logic that can drive the correct tax rates for transactions between entities that belong to the same VAT group number can easily managed by setting the registration status of both parties involved, this is for both AP and AR. When a new company is added to the VAT group then their registration status is changed and automatically the correct tax logic will apply. This means that the correct Legal Entity has to be chosen each time which is a manual process. This is a simple and future proofed solution. There is a work around and that is to create rules linked to the balancing segment value of the transactions taking place together with the registration status of the supplier/customer but whenever there is a new supplier or customer added then new rules are needed making this a maintenance nightmare and to be avoided when possible.

Migrated Data

When data is migrated into the newly created ERP solution, it is usually assigned to an operating unit (for Sub ledger data). If only one operating unit is used for multiple legal entities then at a later stage, it is far more difficult to pull that data out if it needs to be separated at a later stage, if the legal entity is sold off for example.

Reporting

With multiple operating units, the reports can be run by operating unit and thus give another level to split the data out to make the reporting easier to see and also reconcile.

Intercompany

Whether drop shipments or using AGIS, having multiple operating units makes it far easier to create intercompany transactions. If only one operating unit is used then intercompany transactions are limited using just one operating unit and the ship from and the ship to.

Secondary Ledgers

If you have an Operating Unit that has both France and Spain for example, you will need to create a secondary ledger for France using the fiscal CoA. This means that when you post your transactions to the secondary ledger, you will also be posting the Spanish transaction too so a custom process would be need to filter out the Spanish values from going to the French secondary ledger.

Sequencing

Some countries, like Italy, by law require sequencing to be gapless and on every transaction generated. Having only one Operating Unit makes it easier to generate the correct sequence number for the transactions.

More than one Legal Entity per country (Intercompany)

When an intercompany AP transaction is created, no Ship-To information is brought in, nor is the 'Customer Taxpayer ID' changed. This means that it is not possible to calculate the correct tax and only the location linked to the operating unit (bill to) is available to calculate taxes.

One Operating Unit:

The evidence above demonstrates the areas that will cause issues if you are trying to use just one operating unit instead of one operating unit per country per legal entity. But all of the scenarios above can be overcome with customisations, SLA or workarounds. The decision to make is to decide if it worth all the extra setup, testing and on-going maintenance in the future for the sake of having less operating units when the whole point of R12 in Financials is to make it easier to have access across multiple Operating units with MOAC!

Also bear in mind that you may be able to successfully go live but then when it comes to patches, support or future upgrades, all those customisations and workarounds will only cause further problems. Why create custom processes, changes to SLA and workarounds when standard functionality already exists to do the task!

This WHITEPAPER was produced by eBiz Answers Ltd. We hope it was helpfull.
For further Whitepapers or advice visit: **www.ebizanswers.net**

eBiz Answers

eBiz Answers Ltd. WHITEPAPER: Oracle R12 – One or multiple Operating Units?. Copyright 2014.

7