Tax Assurance

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Preface

In 2008, representatives of the Ministry of Finance in the Netherlands and of the big four accounting firms asked the Fiscal Institute of Tilburg University to explore the possibilities of incorporating the subject of Tax Assurance in its educational master programs. Certainly, this was not an easy challenge since the topic of Tax Assurance is new and therefore largely unexplored on a scientific level. It is also by its very nature multi/disciplinary and can only be dealt with in an international comparative perspective.

In 2010, Tilburg University decided to implement a Tax Assurance program in its master Tax Economics. In 2011, we started with a profile Tax Assurance which was immediately a success. The profile consists of two electives (Tax Assurance I and II) plus extra requirements for the master thesis. Upon completing the profile, the student receives a reference on his or her grade list.

The program, coordinated by dr. Ronald Russo, is currently running for the fourth year. All aspects of Tax Assurance are treated in the lectures. Many disciplines are involved, such as accounting (internal control, tax accounting, audit), management, governance (legal, business and ethical aspects), tax policy (by companies and countries), formal tax aspects (relationship between tax authorities and companies). By inviting specialized guest lecturers of the tax authorities, tax advisors and (multinational) companies, students can get a firm theoretical and practical grip on the different subjects. In this way, the students get a balanced view of the problems involved. The program has been run successfully. But it has also led to much research output from the Fiscal Institute of Tilburg University. The most notable recent publication is this book on Tax Assurance. It is the first comprehensive publication on this subject both from a national and from an international perspective. Many guest lecturers and colleagues from the Fiscal Institute of Tilburg University as well as from other universities, tax firms and the tax administration have contributed to it. For all this, I would like to thank and congratulate the authors heartily. Especially, I would like to thank dr. Ronald Russo, who has also done the planning and editing of this book.

Professor dr. Peter Essers

Head of the Department of Tax Law of Tilburg Law School, January 2015
1. Definition and overview

Assurance is primarily an accounting and auditing term with a distinct meaning in those fields of practice, most commonly in relation to the commercial accounts of a company. It is not a common term in taxation, or at least it did not used to be. In the International Auditing and Assurance Standards, Handbook of International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements, 2012, volume 1, p. 16, an Assurance engagement is defined as follows:

An engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria.

In a narrow perspective tax Assurance could be viewed as Assurance on the tax position in the commercial accounts, so that users of those accounts have more confidence in the correctness of it. In this book we view Tax Assurance in a wider context: in our view everything concerning the process of taxes in a company belongs to the field of Tax Assurance. Not just how taxes end up in the commercial accounts (tax accounting), but also (tax) risk management, internal control, management control, corporate governance, tax policy, relations with media, relations with tax authorities, ethical sides of taxation and audit are relevant for Tax Assurance in a broader sense and are therefore present in this book.

The different relevant sides of Tax Assurance as mentioned above are handled in different chapters, each by an author or authors who have expertise in that particular field. Most authors are also lecturer or guest lecturer in the Tax Assurance program of Tilburg University and publish on the topic regularly.

We start the overview of Tax Assurance by looking at processes in a company in general. Generally speaking every process in a company, especially if it may contain risks, must be managed and controlled by the management. These days control is usually effectuated by installing and maintaining systems that can provide such control (identify the risks involved and manage it following established policy). Chapter 2 of this book written by Arco van de Ven is therefore dedicated to risk management in general and the relationship with internal control systems. The history of risks and the reactions of companies and regulators are reviewed critically.
and illustrated with a look at frauds in the past and the recent past. The reaction primarily seems to focus on regulating: first the accounts, then the accountants and then the auditors. Whether this ultimately leads to more assurance, remains to be seen.

The characteristics of an internal control system are greatly influenced by the input, the choices made in the designing of it. The risk appetite of a company for instance determines how much risk a company is willing to take which in its turn (co)shapes the relevant procedures of the internal control system. This applies in general, but also specifically to taxes. The choices regarding the input of the control systems of a company are governed by their own rules and regulations and deal with the issue of how to manage a company. These regulations include the various corporate governance codes in various jurisdictions that, incidentally, all demand an internal control system as a prerequisite for good governance. Issues like ‘tone at the top’ and whether or not to have ‘tax principles’ are important issues that transcend traditional corporate governance debate and move into the field of ethical standards of behaviour. Therefore the fields of Corporate Governance and Ethics are dealt with in Chapters 3 written by Ronald Russo and Jan van Trigt and 4 written by Richard Happé respectively.

Combining the knowledge of risk management and internal control with corporate governance and ethics will lead to a system to control the risks within a company: a Business Control Framework. The part of this framework that deals with taxes is commonly referred to as the Tax Control Framework (TCF). In Chapter 5 Robbert Hoyng, Nathan Andrews and Mark Kennedy work out such a model: a tax operating model; they describe what a perfect system would look like or should at least entail. In this Chapter it becomes clear that the tax function must be linked to the other systems of the company, both with data and people. The influence of, for instance, new forms of information technology that enable new and better ways to store and use data is also apparent.

In Chapters 6, 7 and 8 an important element of Tax Assurance – the relationship between a company and the tax authorities – is looked at more closely. These chapters build on the previous chapters as the tax authorities themselves also use risk management techniques in applying their scarce resources to where they are most effective. The tax authorities can take the internal controls of a company into account in the choices they make. Since internal control is usually fundamentally different in large companies (where ownership and management are usually not in the same hands) and small and medium sized companies (where ownership and management usually are at least partly the same persons), the tax authorities in principle have a different approach for these categories of companies. Chapter 6 written by Robbert Veldhuizen is dedicated to large companies, whilst Chapter 7 written by Bas Herrligers looks at small and medium sized companies. The concepts of horizontal monitoring, enhanced relationships and cooperative compliance as new ways for tax authorities to interact with companies are dealt with in detail for each category. In particular the position of intermediates in taxation (accountants and tax advisors) is viewed as they play a major part in the application of cooperative compliance for small and medium sized companies. The system of the Netherlands is viewed in
more detail on this topic since it is the only jurisdiction where cooperative compliance actually works with small and medium sized companies.

In Chapter 8 some formal tax issues are discussed by Hans Gribnau, such as the principles of equality and fair play, procedural law and the legal boundaries of cooperative compliance systems. Cooperative compliance as such is not embedded in law as it is a way of supervision that commonly falls under the executive competence of the tax authorities. Apart from that: it is a relatively new strategy that has barely led to applicable case law. This can lead to uncertainty within companies regarding their exact tax liabilities and obligations, an undesirable situation for all parties involved. The main pitfalls and uncertainties are therefore dealt with in this chapter.

In Chapter 9 the result of risk management, internal control and the TCF for the commercial accounts is viewed in more detail by Eveline Gerrits: tax accounting. Tax accounting deals with the impact of taxes on the commercial accounts: the balance sheet, the profit and loss account and disclosures. Strictly speaking this is the field of accountants (ruled by accounting standards such as IAS 12), but the content of the issue is taxation, so this is an area where accountants and tax experts meet. This last statement is true for most aspects of Tax Assurance as many fields of expertise are needed to come to a reasonable level of assurance. In this chapter there is also room for the position of other taxes than corporate income tax (as they can also have significant impact in the commercial accounts), the relevant disclosures and new developments such as country by country reporting.

In Chapters 10, 11 and 12 the general content of the first chapters is applied to the three most important categories of taxes. The general set up as discussed in chapter 5 is now made more specific for different categories of taxes. To be in control of tax means something different for wage taxes than value added taxes or corporate income taxes. In practice the general TCF is often divided in specific frameworks for each category. These categories are therefore treated separately each in its own chapter. In Chapter 10 Elmer van Lienen and Marieke Louwen take the reader through the field of wage taxes and related contributions; they look at the specific challenges these taxes pose to be in control. An important issue here is that the controls for these taxes must be closely integrated with other functions of the company, especially the general payroll function. The main risks for this category of taxes are also covered. In Chapter 11 the emphasis is laid by Edwin van Loon on indirect taxes and similarly as with wage related taxes the controls for indirect taxes must be coordinated with the other functions of the company such as sales and finance. As in the previous chapter the main risks specific for indirect taxes are viewed in more detail. In chapter 12 Eelco van der Ende and Eric van der Stroom tackle control on corporate income taxes that require yet other forms of coordination (primarily accounting and finance). The main risks are discussed and also ways to manage these risks are provided. From all contributions on specific tax categories it becomes clear how difficult it is to manage the complete field of taxation within a company. Another common observation is that they all require the tax function to be integrated into the rest of the company, although the focus of which parts are most essential can differ per category.

It gets even more difficult if a company tries to integrate controls for different purposes or risks. In Chapter 13 such an attempt is made by Irene Burgers and Jeltje
van der Meer-Kooistra. They have chosen the subject of transfer pricing, perhaps the single greatest risk for multinational companies in the area of corporate income taxes. They look into control frameworks for transfer pricing and management control and research whether these frameworks could (to some extent) be integrated. Their conclusion is that to some extent, this is possible, but differences are most probably unavoidable. For instance: for taxation purposes the ‘at arms's length’ principle broadly speaking demands that within a multinational company the profits are allocated to affiliated companies as if they were unrelated parties each with their own profit. For management control purposes it might be useful to look at a company and its management just from a cost perspective and not a profit perspective. These two perspectives clash and are hard to reconcile.

The last chapters are dedicated to audit: the audit of taxes (in the process of finalizing the commercial accounts) in Chapter 14 written by Lees Wesdorp and the tax audit by the tax authorities in Chapter 15 written by Joost Engelmoer. The essences of audit are the same for both forms of audit and are dealt with in chapter 14. The remaining part of this chapter is dedicated to the process of auditing the tax paragraphs of the commercial accounts. In Chapter 15 the essences of audit from Chapter 14 are used to build up to the specifics of an audit by the tax authorities and especially its interaction with Tax Assurance. It is interesting to see that while both forms of audit are based upon the same principles they each have their own way of dealing with the problems presented.

The field of Tax Assurance is young and developing fast. New techniques in auditing and testing made possible by further developments in information technology will change the way in which control systems function. The international attention for and focus on tax avoidance is still growing and will lead to all sorts of new developments such as more detailed tax principles to which companies can be held accountable and more cooperation between different jurisdictions. With this book we hope to create more insight into the diverse field of Tax Assurance in the broad sense as we understand it.