

TAX RISK AND CONTROLS - MARCH 3, 2009



## Overview

- Areas of uncertainty
- Cause of areas of uncertainty
- Risk and quantification relation to uncertainty
- Corporate risk appetite and alignment of risk to corporate strategies
- Mitigating controls

## Areas of uncertainty

### Application of tax laws

- Interpretation bulletins, Windows articles, Roundtable commentary
- Cases not yet resolved or heading to higher court
- Treaties not in-force by both parties
- Substantively enacted and minority governments

### Actual fact situation

- Inaccurate or insufficient information available

### Functionality of information system

- Manipulation of accounting information
- Consistency of accounting policy application

### Staffing Considerations

- Inexperience and/or gaps in technical knowledge
- Overworked and/or insufficient time

# Causes of uncertainty

## Routine

- Routine processes such as monthly, quarterly and year end provisions have embedded uncertainties.
- Typically the “known unknowns” .

## Non-Routine

- Non-routine processes such as acquisitions, divestitures and /or significant tax planning structures.
- The “unknown unknowns”.

## Tax Planning

- Represents both routine (claiming carry forward losses) and non-routine.
- Depends on how often the specific type of planning occurs and whether staff is comfortable with the steps required to complete the implementation of the tax plan.

## Risk and Quantification of Risk

- Quantifying the risk (and opportunity) assists the tax department in being able to present a tangible item to senior management, and in certain cases the board.
- Consistent measurement techniques should be applied to support decision making.
- Tax risk can be quantified but also has qualitative aspects which should not be overlooked.
- Consideration should be given not only the pure financial impact of the risk but ancillary costs associated with regulatory and reputational exposure.

## Corporate Risk Appetite

- The tax department should have policies in place which have been approved by senior management (and board depending on hierarchy of corporation).
  - Mandate of tax department – minimise tax risk, look for tax saving opportunities to improve performance, etc.
  - How is tax department evaluated?
  - When, to whom, at what dollar amount, and frequency of presenting tax risk and opportunities?
- Tax department's mandate is aligned with the overall corporate strategy.
  - Corporate expansion discussions occurring without tax at the table.
  - Global contraction of business but tax is not trying to minimise foreign taxes or prepare for a retraction of foreign operations.

## Tax Controls

- **Ensure source information gathered from the accounting and other external departments is accurate.**
  - Does your tax process ensure that raw data is referenced back to the trial balance to ensure there are no material differences?
- **Ensure tax rates used for current and future tax calculations are correct.**
  - Does your tax process ensure that rates used in calculations have been checked to an external source such as a current version of *Income Tax Act* or taxing authority web site (domestic and foreign)?
- **Ensure the accuracy of the tax calculations.**
  - How does your tax department keep abreast of any changes in domestic and foreign tax legislation? Does your tax process ensure that calculations are correct by re-calculating material numbers? Does your department restrict access to spreadsheets used for calculations? Are changes made to spreadsheets tracked and reviewed separately to ensure errors do not occur?

# Tax Controls

- **Ensure that tax contingencies are adequately supported.**
  - Does your tax process ensure that every contingency item is supported with a dollar amount, a related taxation year and the rationale for the contingency?
  - Does your company have to comply with FIN 48 requirements?
- **Ensure the book to actual (“BTA”) adjustment has been made.**
  - Does your tax process ensure that two separate adjustments are recorded (i) prior year’s tax provision estimate to tax return filed adjustment and (ii) prior year’s tax return filed to the assessed amount?
  - Furthermore have you considered why there are significant differences (if any) and can the provision process be improved to reduce these adjustments.

# Tax Controls

- **Ensure inputs for future tax balances are accurate and reasonable.**
  - The decision of whether and where (short or long term) to record a future tax asset/liability may be partially based on the company's revenue forecast in specific jurisdictions, financing plans, planned acquisitions and divestitures, etc.
  - Does your tax process ensure that tax is involved in these strategic discussions and has the most current information?
- **Ensure that a Tax Plan Implementation Review is performed.**
  - Does your tax process ensure that tax plans implemented have been appropriately authorized, implemented and measured?

## Tax Controls

- **Ensure that tax entries are properly authorized and posted correctly to general ledger and tax accounts.**
  - This has two parts as payments into and adjustments between tax accounts (taxing authority accounts) should be properly authorized and reconciled on a monthly basis to ensure balances correct for each legal entity and taxation year.
  - The second part is to ensure that the journal entries made to record the payments, adjustments, accruals, and expense, etc are properly authorized and the general ledger accounts reconcile to tax working papers.

## Tax Controls

- **Ensure that the income tax balances are recorded according to generally accepted accounting principles.**
  - Does your tax process ensure there is adequate documentation to support that taxes are recorded correctly?
  - How does the tax department keep abreast of changes to accounting for its domestic and foreign companies?
  - Have accounting tax policies been approved by the chief financial officer and agreed to by external auditors?
- **Ensure that all tax-related figures used for public dissemination have been agreed.**
  - Does your tax process ensure the tax department reviews and agrees all other tax-related figures in the MD&A, annual report and annual information return?