UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
MANAGE THE TAX FUNCTION

Control practices

The following control objectives provide a basis for strengthening your control environment for the process of managing the tax function. When you select an objective, you will access a list of the associated business risks and control practices. That information can serve as a checklist when you begin reviewing the strength of your current process controls.

This business risk and control information can help you assess your internal control environment and assist with the design and implementation of internal controls. Please note that this information is at the generic business process level and many companies will need to go beyond generic models to address the specific business processes that support the financial and nonfinancial disclosures being made. You can combine the insight of this business risk and control information with your industry-specific knowledge and understanding of your company's environment when conducting internal control assessments and designing and implementing recommendations.

Effectiveness and efficiency of operations

A. The income tax provision is calculated properly.
B. The income tax provision calculation is supported adequately.
C. The income tax provision classification is supported adequately.
D. The deferred tax asset is valued properly.
E. Tax reserve balances are adequate.
F. Tax reserve balances are supported properly.
G. Transactions and data relevant to the calculation of indirect taxes are identified in a timely manner.
H. Taxes are reported and remitted properly and in a timely manner.
I. Senior management is informed of and understands significant tax issues and positions.
J. Tax planning is consistent with corporate goals and values.
K. Internal and external tax communications are consistent with corporate policies and direction.

Reliability of financial reporting

A. Tax accounts are properly stated in the general ledger.
B. Approved general ledger adjustments are input for processing completely and accurately.
C. Approved changes to standing data are input for processing completely and accurately.
D. Tax disclosures and reporting are complete and accurate.
E. Unauthorized access to the accounting records is deterred and detected.

Compliance with applicable laws and regulations

A. The company complies with tax laws, regulations, and judicial decisions.

Effectiveness and efficiency of operations

UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
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A. The income tax provision is calculated properly.

Business risks

- Income tax provisions will be calculated improperly, leading to inaccurate financial statement disclosure.

Control practices

1. Document the process for preparing and reviewing the tax provision.
2. Require knowledgeable tax personnel to maintain a record of permanent differences and credits, reviewing it regularly for completeness and accuracy.
3. Establish a procedure to identify and maintain updated tax rates for all jurisdictions.
4. Prepare rate reconciliations for each jurisdiction in a timely manner, and match material components with source documents.
5. Identify promptly transactions generating permanent differences.
6. Promptly inform those preparing the tax provision of the tax implications of all non-routine transactions.
7. Involve the tax department in major or unusual business transactions, such as acquisitions and entrances into major new jurisdictions.
8. Ensure that appropriate personnel approve changes to any system or spreadsheet used in computing the tax provision.

B. The income tax provision calculation is supported adequately.

Business risks

- The tax provision audit trail will not sufficiently support the provision calculation.

Control practices

1. Record properly any transaction that generates permanent differences.
2. Maintain sufficient schedules to support the calculation of current and deferred tax provision by jurisdiction.
3. Prepare a reconciliation of provision to actual return in a timely manner and record differences properly.
4. Implement controls to determine if profits from foreign operations are either permanently reinvested or repatriated and identify any differences between the equity value and tax basis that may signal the need to pay deferred taxes.

C. The income tax provision classification is supported adequately.

Business risks
- Tax provisions will be classified improperly.
- The tax provision classification will not be supported adequately.

Control practices
1. Analyze general ledger asset and liability accounts to quantify and accumulate differences in book and tax basis to reconcile deferred taxes.
2. Maintain a record of general ledger accounts that affect equity and other comprehensive income (OCI) items.
3. Ensure that management reviews all cross-border transactions for transfer pricing implications, including arm's-length prices and intercompany transaction compliance with transfer pricing regulations.

D. The deferred tax asset is valued properly.

Business risks
- Deferred tax assets will be valued improperly.

Control practices
1. Require management to analyze and regularly review deferred tax asset recoverability for each jurisdiction.
2. Require management at appropriate levels to provide internal corroboration supporting the calculation and disclosure of taxes significantly dependent upon management intentions.

E. Tax reserve balances are adequate.

Business risks

- Tax reserves will not sufficiently cover actual tax costs.
- Tax reserves will be overstated, tying up more cash than necessary.

Control practices

1. Establish procedures for identifying aggressive tax positions and maintaining adequate reserves in each business unit and jurisdiction to cover potential liability for unsuccessful tax positions.
2. Review exposure calculations with management along with a detailed list of reserves.
3. Periodically update exposure calculations and the detailed list of reserves.
4. Validate plans for tax-driven transactions to ensure that the economic outcomes are consistent with expectations.
5. Periodically document, approve, and validate the objectives for scheduled tax-driven transactions.
6. Ensure that tax authority calculations of tax and interest are reviewed after tax matters are settled.
7. Ensure that any adjustments and procedural changes in response to tax audits are communicated to affected areas in a timely manner.

F. Tax reserve balances are supported properly.

Business risks

- Tax exposure calculations and reserve balances will not be properly documented.
- Financial statement disclosures will not be adequately supported.

Control practices

1. Document exposure calculations and a detailed list of reserves.
2. Document approvals of the changes in the exposures items.
3. Ensure that all footnote disclosures are reviewed and compared to supporting documentation for consistency and are discussed with management.

G. Transactions and data relevant to the calculation of indirect taxes are identified in a timely manner.

Business risks

- Indirect tax calculations will be inaccurate.

Control practices

1. Require knowledgeable tax personnel from the collecting party to evaluate transactions for indirect tax receivables on a timely basis.
2. Require knowledgeable tax personnel from each paying party to evaluate transactions for indirect tax obligations on a timely basis.
3. Require knowledgeable tax personnel to identify and reevaluate significant changes to transactions.

H. Taxes are reported and remitted properly and in a timely manner.

Business risks

- The company will incur penalties from tax authorities because taxes are not reported properly or in a timely manner.
- The company will incur penalties from tax authorities because taxes are not remitted properly or in a timely manner.
- Taxes reported and remitted will not properly reflect tax audit findings.

Control practices

1. Require knowledgeable tax personnel for the collecting party to prepare and maintain a required remittance schedule to ensure timely accrual and remittance of taxes due.
2. Require knowledgeable tax personnel for each paying party to prepare and maintain a required remittance schedule to ensure timely accrual and remittance of taxes due.
3. Ensure that tax payments are reviewed and approved by the paying party's tax director or appropriate equivalent.
4. Respond to all tax audit findings and recommendations completely and in a timely manner.
5. Implement action plans to address tax audit findings and recommendations.

I. Senior management is informed of and understands significant tax issues and positions.

Business risks

- Senior management will not understand significant tax issues and positions.
- Senior management will not be able to speak intelligently to the public about the company's tax-related activities.
- Tax activities will not align with overall corporate objectives and values.

Control practices

1. Require regular communication from the tax department to senior management documenting the tax department's planning objectives and significant tax issues.
2. Require senior management approval of significant tax strategies.

J. Tax planning is consistent with corporate goals and values.

Business risks

- Tax planning will not align with corporate objectives.
- Tax planning will not be consistent with corporate values.
- The company will engage in illegal activities to enhance the company's tax position.
- Stakeholders will question the company's financial integrity.

Control practices

1. Require approval by management outside the tax department for transactions initiated by the tax department.
2. Require management outside the tax function to approve tax planning opportunities generating tax savings that exceed a specified threshold.
3. Require corporate legal counsel to approve activities involving legal judgment, including the formation of legal entities.

K. Internal and external tax communications are consistent with corporate policies and direction.

Business risks

- Internal tax communications will not reflect the company's actual tax objectives and values.
- Employees will be unaware of the company's tax objectives, values, and rules.
- External communications regarding the company's tax practices will not accurately reflect the company's tax objectives and values.
- Stakeholders will question the company's financial integrity.

Control practices

1. Require an appropriate level of management approval for participation in tax forums, including tax study groups or other organizations that may express public views on tax matters.
2. Establish appropriate review and approval procedures for tax materials or tax presentations that may become public.
3. Communicate the company's mission statement and strategic objectives for the tax function within the company.

Reliability of financial reporting

A. Tax accounts are properly stated in the general ledger.

Business risks

- Postings to tax-related general ledger accounts will be incomplete or inaccurate.
- Tax disclosures will be inaccurate, leading to tax authority penalties or stakeholder mistrust of financial reports.

Control practices

1. Ensure that appropriate tax personnel review and approve all entries made to the tax accounts, including payments.
2. Require appropriate personnel to compare entries to tax accounts to supporting documentation to ensure each entry is complete, accurate, and recorded in the proper period.
3. Prepare detailed reconciliations for both current and deferred tax accounts.
4. Reconcile sub ledgers to the general ledger monthly.
5. Investigate and resolve in a timely manner questionable entries identified in reconciling sub ledgers to the general ledger.

B. Approved general ledger adjustments are input for processing completely and accurately.

Business risks

- General ledger adjustments will be made inaccurately, for instance, for the wrong amounts, to the wrong accounts, or in the wrong period.
- Tax disclosures will be unreliable, leading to tax authority penalties or stakeholder mistrust of financial reports.
- Duties will not be segregated adequately, increasing the risk of accounting fraud.

Control practices

1. Compare reports following inputs and updates reports to the appropriate adjustment source documents in a one-to-one check for completeness and accuracy of adjustments input into the system.
2. When batch totals are used, separate input documents into groups. Calculate numerical totals for the quantity of documents, dollar amount and hash items. Compare these totals to reports following inputs and updates, and research and reenter all out-of-balance conditions in a timely manner.
3. Require management at an appropriate level to approve all adjustments.
4. Ensure that management's review of adjustments includes an examination of source documentation.
5. Ensure that discrepancies identified in management's review of adjustments are resolved.
6. Segregate the following key functions: 1. accounting and maintenance of detailed tax records; 2. approval of tax amounts, including provisions, schedules, and records; 3. cash receipts; 4. cash disbursements; 5. bank reconciliations; 6. approval of bank reconciliations; and 7. general ledger functions.
7. Investigate and resolve exceptions to segregation-of-duty controls.

C. Approved changes to standing data are input for processing completely and accurately.

Business risks

- Standing data will be incomplete or inaccurate.
- Tax disclosures will be inaccurate, leading to tax authority penalties or stakeholder mistrust of financial reports.
- Duties will not be segregated adequately, increasing the likelihood of accounting fraud.

Control practices

1. Require that an appropriate official approve changes made to standing data prior to input.
2. Require sufficient documentation to support each change made to standing data.
3. Compare reports following inputs and updates to appropriate source documents for the change, in a one-to-one check for completeness and accuracy. Resolve discrepancies and subject the reentered data to the same control procedures.
4. Configure the accounting system to produce a report of changes in specified types of standing data or changes falling outside defined parameters.
5. Configure the system to accept specified types of changes only after receiving appropriate management approval.
6. Require personnel responsible for standing data to regularly review the data and enter any required changes using standard procedures for changing standing data.
7. When batch totals are used, separate input documents into groups and calculate numerical totals of the quantity of documents, dollar amount, hash items. Compare these totals to reports following inputs and updates and research and reenter out-of-balance conditions in a timely manner.
8. Segregate duties involved in updating of standing data from those required for maintaining financial records.
9. Investigate and resolve exceptions to segregation-of-duty controls.

D. Tax disclosures and reporting are complete and accurate.

Business risks

- Tax disclosures will be incomplete or inaccurate.
- Tax disclosures will fail to comply with tax authority requirements, increasing the likelihood of adjustments and penalties by tax authorities.
- Stakeholders will question the company's financial integrity.

Control practices

1. Assign appropriate resources to monitor current generally accepted accounting principles (GAAP) and tax authority disclosure requirements and to determine the impact of changes in a timely manner.
2. Communicate changes in disclosure requirements to all affected parties in a timely manner.
3. Disclose transactions considered by the IRS to be tax shelters, even though the transactions would otherwise not appear to be tax shelters.
4. Ensure that the determination of the annual effective tax rate for use in quarterly filings is accurate.
5. Ensure that changes to any system or spreadsheet used to accumulate tax data are reviewed and approved.

E. Unauthorized access to the accounting records is deterred and detected.

Business risks

- Access to key systems will not be controlled adequately, increasing the risk of accounting fraud.
- Inaccurate accounting records will lead to inaccurate tax disclosures.

Control practices

1. Use access controls, such as user IDs and passwords, specific to each application.
2. Ensure that multiple failures to log on to an application invalidate a user ID and result in an exception report.
3. Require management to investigate and resolve all exceptional items reported.
4. Require formal authorization by personnel responsible for specific accounting records for access to the application.
5. Require management to review access rights periodically to ensure that only authorized individuals have access and that segregation of duties is maintained. Ensure that exceptions to access controls and segregation of duties are investigated and resolved.

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Compliance with applicable laws and regulations

A. The company complies with tax laws, regulations, and judicial decisions.

Business risks

- The company will fail to comply with tax laws, regulations, and judicial decisions, increasing the likelihood of adjustments and penalties by tax authorities.
- Stakeholders will question the company's financial integrity.

Control practices

1. Assign appropriate resources to monitor current changes in laws, regulations (including GAAP), and court decisions that affect tax provisions.
2. Assess and document the impact of tax rule changes on the company's tax practices.
3. Establish a formal plan for communicating tax rules changes to appropriate personnel, both within the tax function and in other departments.