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Issue 74, October 2024

Having a VAT control framework can help reduce tax audit disruption

In recent years, many jurisdictions around the world have adopted digital tax reporting measures for value-added tax (VAT) reporting. Increasingly, this means that businesses are required to submit VAT data electronically and in real time, leaving little opportunity to correct errors in advance — and allowing for greater tax administration scrutiny.

Many tax authorities now use this information to identify taxpayers, sectors or transactions at a higher risk of noncompliance. Artificial intelligence (AI) may also play a role in analyzing tax data to identify potential audit targets. In some jurisdictions, the risk assessment is also based on the tax governance framework of the individual business and, in particular, how its systems and processes ensure that data flows correctly into its periodic VAT returns. To support this approach, the tax authority may issue detailed questionnaires to businesses about these topics and may use financial audit specialists to test companies' systems.

Taxpayers categorized as "high risk" may then expect more frequent or more detailed tax audits, while "low risk" taxpayers may receive a "lighter touch" or less frequent inspections. The benefits to a business of achieving low-risk status, and maintaining it, therefore, can be significant.

Creating an effective VAT control framework requires cooperation across the organization to design and incorporate appropriate controls suited to the business. If a business is to be treated as "low risk", it should be able to "show" as well as "tell" that it has the right policies and procedures in place. It should also show that these procedures are followed to prevent errors and to remediate issues that do occur. Having detailed and accurate documentation is vital, such as copies of Tax Risk and Controls Matrices, tax policy documents and details of control testing. Reviewing the framework is also key to reflect changes in VAT legislation or tax compliance obligations that may create new risks.

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Contact us for more information

Luis Coronado
EY Global Tax Controversy Leader
luis.coronado@sg.ey.com

Craig A Hiller
EY Global International Tax and Transaction Services Leader
craig.hiller@ey.com

Kevin MacAuley
EY Global Indirect Tax Leader
kmacauley@uk.ey.com

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