ISO Audit Data Collection Standard

Indirect Tax (VAT) extension

Examples and requirements

DRAFT WORKING DOCUMENT – FOR DISCUSSION PURPOSES ONLY

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1 Justification and proposed approach

ISO (the International Organization for Standardization) is a worldwide federation of national standards bodies (ISO member bodies). The work of preparing International Standards is normally carried out through ISO technical committees. Each member body interested in a subject for which a technical committee has been established has the right to be represented on that committee. International organizations, governmental and non-governmental, in liaison with ISO, also take part in the work. ISO collaborates closely with the International Electrotechnical Commission (IEC) on all matters of electrotechnical standardization.

This document establishes common definitions of accounting data elements and provides the information necessary to extract relevant audit data.

2 Introduction

This document is applicable to the bridging of understanding among auditors, auditees, software developers and IT professionals, and creating a mechanism for expressing the information, common to accounting, in a manner independent of accounting and ERP systems. The reasoning behind this is:

1. Indirect taxes and customs duties cover a wide area with diverse laws and regulations;
2. ERP systems have found their own ways to process and store specific data (attributes) for indirect taxes and customs duties;
3. Our task is to design a way that meets both challenges and provides at the same time only a limited extension to the current standard (without making any changes). We believe that we have found a solution.

This ADCS Indirect Tax extension has been designed to allow auditors access to data in an easily readable format for substantive testing of system controls and data, using proprietary audit software, as part of a methodology that also provides increased effectiveness and productivity in computer-assisted audit. This ACDS-extension should enable small and medium enterprises ("SME"), but also large companies to provide the requested data in such easily readable format. On the other hand, it should enable auditors to access the data attributes needed to audit a company in the light of indirect taxes.

Based on the ISO/FDIS 21378 document – which can be seen as the base document - it is stated that the ACDS covers the main business modules of accounting and ERP systems and the main business processes in the enterprise production supply chain. The ADCS has eight modules: Base (BAS), General Ledger (GL), Accounts Receivable (AR), Sales (SAL), Purchase (PUR), Accounts Payable (AP), Inventory (INV) and Property, Plant and Equipment (PPE).

Next steps are to further complete the extension and to validate these against common and less-common data attributes applicable in multiple countries.

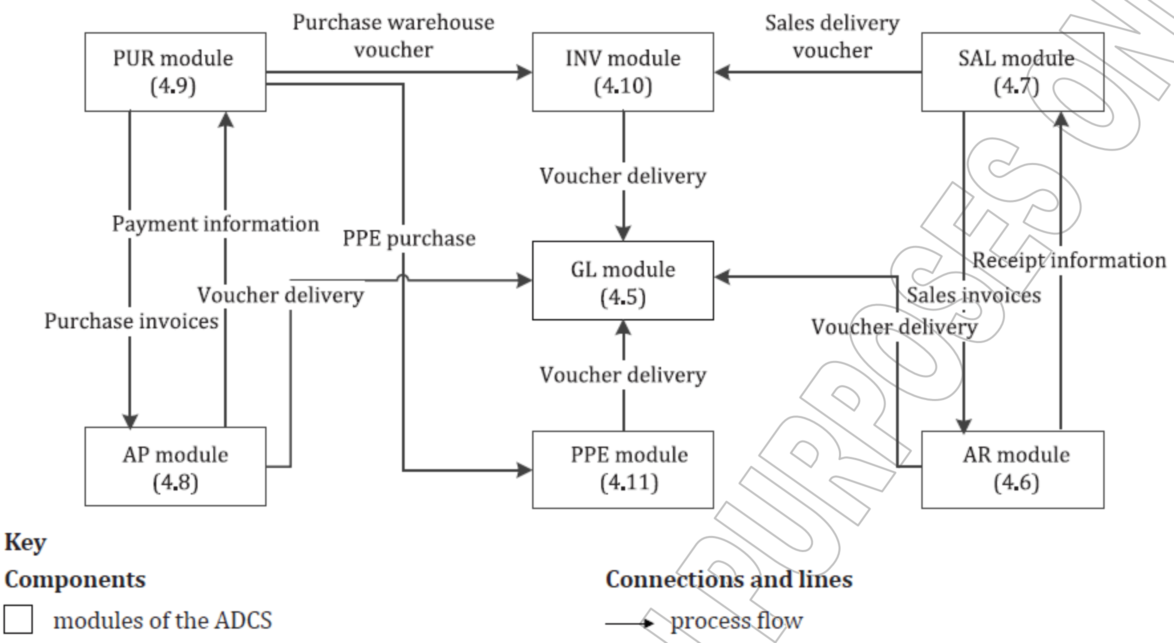

Figure 1 — Business modules in the ADCS

With this Indirect Tax extension local authorities and auditing companies should have an additional tool to determine whether the audited company has paid the correct tax at the right time, in accordance with domestic tax legislation. The auditor must obtain and evaluate the available audit evidence as part of the audit assurance process in order to reach an opinion as to whether or not a tax return is correct.

3 Indirect Tax ("VAT/GST") requirements

3.1 Introduction

In this chapter, we will work out the generic aspects common to indirect taxes that need to be supported by the ADCS and the extension. Once we have the overview, we can determine which elements are inherently supported by ADCS and which need a place in the extension.

3.2 VAT/GST requirements

A good starting point to list the generic elements is the OECD report [*Consumption Tax Trends 2020-VAT/GST and Excise Rates, Trends and Policy Issues*][1]. This report is compiled by a group of experts, is updated annually and provides an overview of the main characteristics. It would seem sensible to use this as a lever.

Based on the OECD report it can be recognized that for a tax jurisdiction, the applicable tax treatment (taxed or exempt) and tax rate might differ. At a **jurisdictional level***, the actual tax treatment may result from the tax rate applicable to the:

- **Product/item**: e.g. reduced rate for food, standard rate for telecommunications and super rate for luxury goods;
- **Business Partner**: e.g. standard rate for regular consumers, zero-rate for embassies/UN-organizations;
- **Place of supply:** zero-rate/exempt for supply abroad, reduced rates for specified regions, zero-rate for free trading zones, VAT warehouse;
- **Size of the business of the taxpayer**: e.g. regular versus small-scale taxpayers;
- **Type of industry**: for certain types of industries specific rules might apply.

The above should be suitable for all taxes based on accounting entries, even down to line level, and encompasses both direct and indirect taxes. However, the determination of tax liability of direct and indirect taxes may require information not normally found in an accounting system. For the ADCS we should classify additional characteristics into a number of categories/aspects, but for our purpose we need to add some categories which are not explicitly described but needed for our purpose. The suggested additional categories** to further explore are:

I. Taxable transactions: Both goods and services;
II. Taxable amount and rates: VAT rate structures and VAT exemptions, as they could relate to the **Business Partner**, **Place of supply** or the **Product/items;**
III. Taxable amount and rates: Application of margin schemes;
IV. Tax point date;
V. Deductions: Mechanism of charging VAT/GST on sales and allowing business to deduct input tax;

We have included a more detailed description of these categories (and why they are relevant) in Annex II to this document.

[1] https://www.oecd-ilibrary.org/taxation/consumption-tax-trends-2020_152def2d-en

** see Annex I for the examples of the Jurisdictional tables*

*** see Annex II for the examples of these additional categories*

3.3 Justification for an extension

In principle tax coding in ERP (and accounting) systems are a subdivision of a tax type mentioned in table 42. The information stored in such tax codes could provide insight in the above required additional categories. However the invoice line details in table 82, the tax information per line contains only a tax type and tax amount. In effect, the following data is stored for audit purposes in relation to a transaction in Table 82:

		Information stored in Table 82	
Scenario	**Type of transaction**	**TaxType1**	**TaxAmount1**
1	Sale of goods (for EUR 100) in the Netherlands subject to 21% VAT	Value indicating NL VAT	21
2	Export sale of goods (for EUR 100) from the Netherlands, subject to 0% VAT	Value indicating NL VAT	0
3	VAT exempt supply of a service (for EUR 100) in the Nethelands	Value indicating NL VAT	0
4	VAT taxable supply of service (for EUR 100) provided by a Dutch supplier to an EU customer outiside the Netherlands, VAT reverse charged to the customer	Value indicating NL VAT	0

Currently the ADCS only provides invoice lines based on table 82, where the tax information per line consists of the tax type and tax amount. As illustrated above, the effect of this is that three scenarios that are fundamentally different from a VAT-perspective (Scenarios 2, 3 and 4 above), yield the same audit information. The lack of granularity that this provides could cause an issue if the auditor of the transaction cannot reconstruct whether exemption, reverse charge, 0% has been applied. This could also be extended for the other additional categories.

One way to facilitate this would be to change level of connection and add tax code to table 82, but this would entail a change to the standard, and the additional information besides the tax type and tax amount is only particularly relevant in case the audit covers the correct VAT treatment of transactions.

We therefore suggest to support an extra level of detail with the proposed extension by linking additional characteristics to the invoice line level. For each invoice line, various characteristics can be linked that way (e.g. source system tax code, (multilanguage) description, VAT recovery ratio, goods/services code, etc.).

4 Technical Tables Design

In order to make the concept work for nicely for ADCS we need to:

- Link the observation to entries in other tables
- Split each variable in two columns and define
- Applicable common entries for the variables
- Set up a list of values (as an example)
- Link each variable value to system value

[TO BE FURTHER DEFINED BASED ON INPUT FROM THE EXPERT GROUP]

5 Audit Examples

5.1 Purpose

The purpose of the extension is to allow auditors to access data attributes that are not included in the standard scope if the ADCS, but are needed to verify the indirect tax treatment of transactions. This section uses some examples to illustrate some of those data requirements, and how they could be addressed by the extension.

5.2 Exempt items (e.g. children's wear)

In the Netherlands children's wear is subject to standard rate for VAT, in the UK there is an exemption. Let's suppose that first transaction in 2021 is to NL customer and second transaction to UK customer.

Transaction Document ID	Transaction Document Line ID	Characteristic Type	Characteristic UOM Code	Characteristic Value	System Value
202100021	001	NL_VAT_item_status		S	1
202100022	001	GB_VAT_item_status		E	0

5.3 Exempt items (e.g. supply to embassies)

In a considerable number of countries, deliveries to embassies or consulates are exempt from VAT. In ERP systems, this is controlled by the status of the customer. Suppose the third transaction is a supply to an embassy based in Brussels, the fourth is a supply to a regular customer in Belgium and the fifth a B2B-supply from a Belgian warehouse to a French customer.

Transaction Document ID	Transaction Document Line ID	Characteristic Type	Characteristic UOM Code	Characteristic Value	System Value
202100031		BE_VAT_businesspartner_status		E	5
202100032		BE_VAT_businesspartner_status		S	1
202100033		BE_VAT_businesspartner_status		K	

5.4 Layering indirect taxes (VAT and energy tax)

It is common that a number of indirect taxes are levied within the same jurisdiction. In some cases the taxes are designed so that only one applies at the same time, but in many cases they are 'stacked' or 'layered', with multiple taxes applying on the same invoice. And example of this can be seen with supplies of electricity, where in addition to VAT an energy tax is applicable in certain countries. In the EU, this energy tax is typically part of the taxable amount for VAT, making it a necessary attribute for auditors.

Let's consider the example of a Dutch electricity provider, supplying electricity to a charge point operator for electric vehicles. The supply is subject to a reduced Energy Tax rate and exempt from the Sustainable Energy Surcharge ("ODE"). The supply is subject to the regular NL VAT rate.

Transaction Document ID	Transaction Document Line ID	Characteristic Type	Characteristic UOM Code	Characteristic Value	System Value
202100041		NL_EnergyTax_item_status		R	1
202100042		NL_EnergyTax _amount	EUR	0.04	0.04
202100043		NL_ODE_item_status		E	0
202100044		NL_ODE_amount	EUR	0.00	0.00
202100045		NL_VAT_item_status		S	1

5.5 Supply of alcoholic items subject to customs control

Let's suppose that the auditee is a microbrewery located in Belgium and that for the supply to the French customer, the alcohol percentage needs to be reported. Also this transaction should be reported to the National Office for Statics. The same(!) table can be used:

Transaction Document ID	Transaction Document Line ID	Characteristic Type	Characteristic UOM Code	Characteristic Value	System Value
202100051		BE_VAT_businesspartner_status		K	
202100052	001	EU_EXC_alcoholpercentage	PERC	0.055	
202100053	001	EU_INTRASTAT_STATVALUE	KG	1,000.00	

6 Annex I

Indirect taxes might be levied on a national bases (e.g. VAT in the EU), but can also be levied on a lower level (e.g. state sales and use taxes, and city sales taxes in the USA). In many cases, these levels are applicable simultaneously, forming a 'hybrid' tax system (apart from the USA, examples of countries charging indirect tax at a national level and at a state/provincial/city level include Brazil, Canada and India)[2]. To deal with this in a meaningful way, it is recommended to introduce the concept of tax jurisdiction.

Wikipedia's definition of jurisdiction[3] is: "is the practical authority granted to a legal body to administer justice, as defined by the kind of case, and the location of the issue".

For indirect taxes, the executive or practical authority can be recognized at various levels. For indirect tax purposes it is necessary to be able to determine the applicable jurisdiction. For this, a table is required which links tax type with tax jurisdiction and country. As a simplified example:

TaxType	TaxJurisdiction	ISOCountry	Description
VAT	AT	AT	Austria
VAT	BE	BE	Belgium
VAT	ES	ES	Spain: mainland
VAT	ES-CN	ES	Spain: Canary Islands
VAT	ES-CE	ES	Spain: Ceuta
CA	CA	CA	Canada
PST	CA-BC	CA	Canada: British Colombia
HST	CA-ON	CA	Canada: Ontario

[2] There are a lot of other cases, for example Spain which has a different VAT regime for Canary Island, Ceuta and Mellila from the main land.

[3] https://en.wikipedia.org/wiki/Jurisdiction

7 Annex II

Each example could be further defined based on the discussion with the expert group, based on local needs and requirements. These examples should be considered as a starting point and could be subject to change.

(I) Goods and services

Goods can be defined for our purpose as any physical or tangible thing[4]. Supply of items other than goods can be classified as services, excluding transfers of cash, property rights and similar items. The distinction between goods and services is important as their tax treatment, determination and/or reporting, might be different.

The current suggested extension for customs only focuses on goods, but for VAT/GST services are relevant as well. The main methods to include services as well are by:

- adding an additional attribute or label the item as goods or services: e.g. Goods Service ID with a restricted domain ['G', 'S'];
- adding a new instance which classifies items as good or services. This instance might include some product hierarchy and/or reporting attributes[5];
- using the attribute Characteristic Type to make distinction between goods and services

There are pros and cons for each option. Suggestion is made to elaborate on this in the near future.

The classification of items as goods or services might differ occasionally per jurisdiction. Decision should be made whether this will be supported too by:

- adding an attribute per jurisdiction, or
- if applicable a country extension / override where needed.

Last but not least, discussion is needed whether it suffice to add a solution for the distinction Goods/Services on item level only. Some ERP-systems are only reporting transactions and will get the data from another source system. Th distinction between goods/services might therefore only be available at the level of

- Sales/purchase invoice line;
- General Ledger line ;
- Tax report line.

To discuss whether to add attributes as well for the defined instances.

[4] Tangible property includes any physical goods. Electricity, gas, heat or cooling energy and the like may be considered as a tangible property for the VAT/GST purposes as well as certain interests in immovable property amongst others. As the actual classification might differ per jurisdiction, an entry in the classification might be jurisdiction specific. The design of the table should The design of the table should take into account that this may be jurisdiction-specific.

[5] Some countries have introduced specific reporting lines on their VAT return to report listed categories of goods or services. Examples include reporting the sales of gold, agricultural products or beer to name a few

(II) VAT rates

[TO BE FURTHER DEFINED]

(III) Place of Supply

For consumption tax purposes, the place of supply of goods or services is the place where that service or delivery of goods is treated as being supplied. This is the place where it's liable to consumption taxes (if any).

The place of supply is mainly based on one or a few of the following attributes:

- Ship-from address
- Ship-to address
- Place of establishment
- Residence (e.g., consumers)
- Plant (e.g., for sale without transport of goods. Can also include place not determined as high-seas - cargo in transport)

To be verified whether which of these attributes are already being defined.

The tax status of a specific location might be relevant in this respect as well. One can think of free-trade-zones, customs warehouses, VAT warehouses and so on.

Example of suggested instance: Tax indicator location / explanatory table

Location	**LocationType**	**Tax Item ID**
1001	plant	2
1002	plant	1
1003	ship-to	1
1004	residence	1
1005	plant	0

Tax Item ID	**Description**
0	Free trade zone
1	Taxed
2	VAT warehouse
....	

(IV) [TO BE FURTHER DEFINED]