

# Elevate Your VAT Control Framework to the Next Level



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# Overview

A strong control environment is crucial for success in today's complex business landscape. A Business Control Framework (BCF) provides a holistic approach to ensuring operational efficiency, compliance, and risk management through structured governance and monitoring. Meanwhile, a Tax Control Framework (TCF) addresses tax-related risks and compliance requirements. Understanding the synergy between these frameworks is vital for organizations striving for optimal governance.

While the BCF offers comprehensive oversight across various compliance areas, the TCF focuses on tax-specific compliance challenges. Insights from the BCF enhance the TCF's effectiveness by addressing unique tax risks, fostering a comprehensive risk management strategy that benefits the entire organization.



## Key Components of Tax Risk Management

### Identification of Tax Risks:

- Regulatory Changes: Adaptations in tax laws and regulations or their interpretations that can impact tax liabilities and compliance obligations.
- Cross-Border Transactions: Challenges associated with international operations include transfer pricing, withholding taxes, and indirect taxes.
- Complex Structures: Intricate organizational frameworks or financial transactions that may attract scrutiny from local tax authorities.
- Operational Practices: Risks stemming from accounting practices, including insufficient documentation and inadequate record-keeping.

# Understanding VAT Risks

Value Added Tax (VAT) poses considerable risks for businesses in intricate tax jurisdictions. Awareness of these risks is essential for ensuring compliance and optimizing tax management strategies. Key VAT risks that organizations commonly encounter include:

- Non-Compliance with VAT laws and Regulations: Ignoring local VAT laws can lead to penalties or legal repercussions.
- Incorrect VAT Classification: Misclassifying goods or services or customers may result in overpayments or underpayments of VAT.
- Inaccurate VAT Reporting: Errors in VAT returns or other VAT-related filings can attract increased scrutiny from tax authorities and lead to penalties.
- Failure to Register for VAT: Failing to register when required can result in accumulating tax liabilities and potential legal as well as commercial consequences. For example, logistics problems when importing goods into a country, as well as subsequent delays and holdups of shipments, can disrupt daily business.
- Errors in VAT Recovery Claims: Mistakes during input VAT deductions can lead to financial losses or increased audits.
- Cross-Border Transaction Management: Misunderstanding cross-border VAT rules can result in double taxation and lost revenue.
- Inadequate Record-Keeping: Failure to maintain proper documentation can complicate audits and tax claims.
- Fraudulent Activities: Any inadvertent involvement in VAT fraud can lead to severe legal consequences and reputational damage.

## VAT Control Framework

A VAT Control Framework is a crucial internal tool for managing indirect tax obligations. It identifies and addresses VAT risks while ensuring compliance with legislation and accurate reporting. A robust framework mitigates risks and identifies opportunities for improvement within the VAT function. The principal aim of a VAT Control Framework is to provide clarity and systematic oversight of VAT-critical processes, ensuring no gaps exist that could lead to financial penalties or excessive tax assessments.

## Current Business Landscape

Transaction complexity is rising in the interconnected global marketplace, especially for multinational companies navigating non-routine transactions. As business models evolve, responsibilities across finance, IT, and supply chain departments intertwine, complicating VAT management.

## Deficiencies in VAT Management

Many organizations struggle with VAT processes, lacking a cohesive strategy to identify and manage risks. When VAT compliance responsibilities are fragmented across departments, inadequate controls can lead to significant financial and reputational consequences.



## Establishing Adequate Control Mechanisms

Organizations must establish a VAT Control Framework to effectively manage their VAT obligations in conjunction with the Business Control Framework (BCF) and Tax Control Framework (TCF). This requires clear administrative guidelines regarding authority and resource allocation for the indirect tax department, as well as well-defined roles and support functions within the department.



## Guidelines for VAT Planning

VAT planning should align with broader business objectives while mitigating compliance risks. A Tax Policy must outline procedures for involving the tax department in significant transactions. Could you set clear criteria for when the tax department must be consulted, especially during critical operational or transactional changes?

## Considering Tax Implications in Operational Changes

Operational modifications necessitate a comprehensive analysis of tax implications to ensure compliance across all business functions.

## Optimizing the Use of VAT Resources

Effective resource allocation is critical for managing VAT risks. Ensuring high-risk areas receive timely intervention is key to successful VAT oversight.

## Benchmarking Risks and Controls

A formalized tax policy clarifies VAT risk parameters and serves as a tool for benchmarking against industry standards. Defined metrics allow organizations to measure compliance readiness and effectiveness.

## Conclusion

A robust VAT Control Framework is vital for navigating today's regulatory complexities. By fostering accountability, optimizing resources, and ensuring coherent governance, organizations can better manage VAT compliance, mitigate risks, and enhance operational success.



# How Can KGT Support You?

## Improve your VAT Control

Framework using KGT's normative benchmarking framework. KGT empowers clients to establish effective VAT control frameworks that enhance compliance and efficiency. Our standardized framework allows for a thorough assessment of your current position, identifying gaps and recommending targeted controls.

Developed by an experienced team that includes former EY Indirect Tax partners and senior VAT leaders, our approach draws insights from industry best practices to address your unique challenges. We provide comprehensive tax consultancy, advisory services, and skilled internal audit support designed for multinational corporations.

Trust KGT to optimize your tax strategy and bolster your financial integrity. We want to help you navigate the complexities of VAT and achieve your organizational goals.

## Check the performance of your VAT risk management with KGT's SAP review

Our systematic evaluation scrutinizes how your organization's VAT processes are configured and managed within SAP, ensuring that your system operates efficiently and complies with local tax laws.

KGT examines your SAP system's VAT settings, including VAT codes, rates, and account assignments, verifying that they align seamlessly with the latest local tax regulations. Our experts will review your tax determination configuration to ensure it accurately categorizes transactions. This includes assessments based on place of supply rules, customer/vendor types, and product/service classifications—no detail is too small.

You gain valuable insights and actionable recommendations by engaging with KGT's VAT specialists during our review process. We empower you to implement best practices effectively, enhancing your VAT management capabilities.

## Check the performance of your VAT risk management with KGT's data analysis

KGT has created an advanced data analysis solution for SAP users. Their SAP add-on automates tax controls and improves the efficiency of control checks, allowing for client-specific adaptations. This add-on extracts tax information for each billing document by considering factors like departure and destination countries, customer and material tax classifications, and applicable tax codes. It aligns with best practices and compares results with SAP's determinations, highlighting discrepancies.

A key feature is the “full flow” check in SD billing, which gives an overview of VAT codes throughout the invoice chain linked to a sales order. This aids in ensuring compliance with local VAT regulations for goods supplied from European warehouses.

For example, intercompany partners Party A and Party B in the ABC flows can track tax determination results across the entire process. Additionally, the cockpit includes a ‘check result’ dashboard with traffic light indicators for adequate health checks.

KGT will analyze data and compile a report detailing the tax determination logic, associated risks, and key findings. This report will also identify the necessary steps to address any existing gaps. If you find our data analysis an invaluable resource for regular assessments, consider securing a license for our solution with an annual subscription.

