

## Avoiding Corporate Tax Icebergs

by Neil Gerard, CPA

**M**anaging risk today has clearly become a priority within every organization and a key part of every CFO's and audit committee member's responsibilities. Organizational risk is far reaching and can impact employee productivity, service, company brand value, and earnings quality. Risk analysis focuses on identifying and evaluating the risk with the greatest potential for loss and the greatest probability of occurrence within an organization. Once these risks are identified, management must work with its advisers to develop controls and processes to ensure that risks are properly controlled, constantly monitor for system failures, and regularly update internal processes to ensure that any risk that does occur is swiftly and properly identified. Taxation is one of the most significant areas of an organization's risk profile.

### Tax Exposure

When assessing tax risk, management should first focus on identifying the types of tax that may lead to exposure if not handled in compliance with established regulatory requirements. These commonly include—but are not limited to—sales and use tax, property tax, payroll tax, Federal and state income tax, international tax, and customs and duties tax. The tax department is responsible for handling both the tax return filing requirements, as well



as preparing the worldwide tax provision for the financial statements. Over the past several years, tax accounting has led to a large number of financial restatements.

### Rules and Regs

With the ongoing legislative changes in Federal, state, and international tax filing requirements—along with the increased level of filing complexity—tax risk is on the agenda of every CFO and audit committee. The Financial Accounting Standards Board's efforts to provide greater transparency in the tax area has resulted in the implementation of ASC 740-10 (formerly FIN 48) requiring uncertain tax positions to be reported in financial statements. Additionally, the Internal Revenue

Service ("IRS") has instituted Schedule UTP, which requires filers to disclose uncertain tax positions on their returns; the phase-in period of which depends on company size, though companies with assets in excess of \$100 million are impacted beginning with the 2010 tax year.

### Processes and Controls

Beyond positions claimed, tax risk may also be associated with the processes in place to prepare a company's tax provision. A major issue facing corporate finance and tax departments is managing available resources. In order to comply with the financial and tax reporting requirements, these departments are

required to significantly increase the amount of documentation and spreadsheet analysis to support quarterly and year-end tax provisions. Further pressure is added by third-party audit firms that need these departments to update memoranda regarding uncertain tax positions so that they may accurately opine on their financial statements.

To more effectively manage restatement risk related to a company's tax provision, CFOs have typically increased the focus they place on their tax departments, developing processes and internal controls that will detect errors and eliminate or reduce the probability of a restatement. Now that corporate executives have a better understanding of the tax processes associated with preparing a tax provision, they understand the risks associated with their uncertain tax positions.

### What the Future May Hold

An interesting byproduct of the added disclosure requirements for Schedule UTP and ASC 740-10 may lead companies to change their overall risk tolerance and limit the number of uncertain tax positions taken in the future. IRS audits, penalties, and potentially damaging public disclosures have quickly changed the landscape for companies implementing tax planning strategies that are not "more likely than not."

An organization's corporate brand, public trust, and integrity can change quickly if an organization does not have a management team dedicated to controlling risk. Risk profiles need to be constantly updated and monitored as an organization grows, changes and operates. Expansion into new countries or markets, reorganizations, and acquisitions

all can change the risk profile of a company very quickly. CFOs must develop a corporate culture for communicating changes so that all departments understand their business' risk profile. Icebergs can be avoided by organizations that have the tools and processes in place to monitor risks both currently and prospectively. ■



Neil Gerard, CPA, is a tax partner at J.H. Cohn. He may be reached at [ngerard@jhcohn.com](mailto:ngerard@jhcohn.com) or 973-403-7995.

## CALIFORNIA

### Los Angeles

11755 Wilshire Boulevard  
17th Floor  
Los Angeles, CA 90025  
310-477-3722

### San Diego

9255 Towne Centre Drive  
Suite 250  
San Diego, CA 92121-3060  
858-535-2000

### Warner Center

21700 Oxnard Street  
7th Floor  
Woodland Hills, CA 91367  
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## CAYMAN ISLANDS

P.O. Box 1748 GT  
27 Hospital Road  
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877-704-3500 x7839

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76 Batterson Park Road  
Farmington, CT 06032  
860-678-6000

### Glastonbury

180 Glastonbury Blvd.  
Glastonbury, CT 06033  
860-633-3000

### New London

125 Eugene O'Neill Drive  
Suite 120  
New London, CT 06320  
860-442-4373

### Stamford

1177 Summer Street  
Stamford, CT 06905  
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## MASSACHUSETTS

### Springfield

One Monarch Place  
Suite 2020  
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## NEW JERSEY

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Roseland, NJ 07068  
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### Princeton

103 Carnegie Center, Suite 311  
Princeton, NJ 08540  
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## NEW YORK

### Manhattan

1212 Avenue of the Americas  
New York, NY 10036  
212-297-0400

### Long Island

100 Jericho Quadrangle  
Suite 223  
Jericho, NY 11753  
516-482-4200

### White Plains

1311 Mamaroneck Avenue  
White Plains, NY 10605  
914-684-2700



877-704-3500  
[www.jhcohn.com](http://www.jhcohn.com)

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