



OECD Presentation

The future treatment of SMEs (small and medium-sized enterprises), the role of tax intermediaries and audits

Good morning, ladies and gentlemen.

Let me take you into the world of future developments concerning the audit and the existence of the audit. The future of the audit can be broken down into two aspects:

1. The need for validated (reliable) information
2. Technical developments

The need for validated (reliable) information will always exist because economics is a behavioural science based on trust. Trust does not just happen, so some form of validation will always be necessary. Without it, the economy will stagnate.

To give you an example: During the past year, cases came to light in the Netherlands where entrepreneurs had made their decision whether or not to supply products based on published annual financial statements, as a way of checking the purchaser's reliability. It was later discovered that these published financial statements were false. As a consequence, the suppliers suffered major losses. What is the underlying point here? Entrepreneurs look for reliability in order to do business. Since the information in these cases did not have to be not validated (compilation), people with bad intentions made use of the opportunities available to deceive the entrepreneurs concerned.

It is a feature of legal entities that entrepreneurs can separate their personal liability from their business activities. However, a legal entity must publish its accountability. Given that in these cases the publication happened without involving a third party, this does not therefore provide sufficient reliability to do business. This demonstrates that the addition of validation (reliability) absolutely does have an important role in the economy.

That means that we do not have to question the reason for the existence of the audit. What we can question, however, is the nature of the validation: the content of the audit.

The underlying question here is whether the techniques and technology can provide reliable information without an actual audit. An actual audit, carried out by a third party. I don't expect that this will happen in the next few years. And my personal opinion is that we will never reach this point. However, the content of the audit will acquire a major element of 'safety' and 'security'. Knowledge of the actual techniques and technology of networks, protocols, firewalls and other security techniques will become increasingly important. Let me focus for a moment on the phenomenon of 'hacking'. This is also linked to our perception of mankind. Often we pay too little attention to this. I always like to refer in this context to a lecture by Dr Andreas Kinneging, a Dutch Professor of Philosophy of Law at Leiden University.

I quote: 'We humans are no angels. We are a long way off achieving that moral level. There is a lot of good in us, but also a lot that is not so good. And also a fair few things that you cannot label as



anything other than bad. We have a light side, but also a dark one. Man is a morally ambivalent being. He is neither an angel nor a devil. He sits somewhere in between'. End of quote.

In terms of safety and security, it will also continue to be important to properly segregate roles and privileges in the digital system. And that also implies that other requirements will be placed on professionals. This may also lead to more collaboration in the audit between multiple professionals. After all, it is not easy to combine all the expertise within one person. That will be a challenge for the near future.

The audit: market (enterprises) & government (taxes)

From the market perspective, it is generally said that the audit is carried out for the benefit of society. To make this easier to understand, I prefer to talk about 'stakeholders' instead of 'society'. This term 'stakeholders' refers to financiers and investors, but also – and we tend to forget this – suppliers, customers, staff, works council, the government and all the authorities involved in the laws and regulations with which entrepreneurs have to comply.

The Tax and Customs Administration, in particular, is becoming a more and more significant stakeholder. It is and will become increasingly important that the Tax and Customs Administration can depend on reliable information flows that also keep a lid on the monitoring costs which are financed using public funds. Checks by the Tax and Customs Administration can also be much more effective. I will return to this later.

If we focus now on the approach of the Tax and Customs Administration, we are dealing with the 'statutory audit' (the market) and the 'tax audit'. The statutory audit targets the true and fair value of total accountability, including the completeness of the revenue recognition.

The tax audit is aimed at the completeness of the tax revenue, with a key underlying aspect being the completeness of the revenue recognition as the basis for the tax revenue.

It would be great if the 'statutory audit' and the 'tax audit' could be interchangeable. In most cases this will not be entirely possible, but it can be achieved to a considerable extent based on common elements. By making use of these common elements it will be possible to make societal costs more manageable. In this case, I would like to address the development of Horizontal Monitoring. This form of monitoring already makes use of this interchangeability. It is important that this is developed even further, particularly in the interests of making societal costs more manageable. There are several countries that are experimenting with Horizontal Monitoring to some extent. From a manageability and cost point of view, making Horizontal Monitoring more professional is a positive development.

From the SME perspective

If we approach the future from the position of the SMEs, we first have to note that there are different regimes for the statutory audit in the various European countries and in the rest of the world. The services performed by intermediaries for SMEs can be divided into three segments:

- Statutory audit
- Voluntary audit
- Compilation



The first two (the statutory and voluntary audits) are equal to each other when it comes to the basis and results of the audit (the opinion). The compilation is obviously different in terms of basis and result. SMEs engage intermediaries to help them fulfil their accountability obligation (annual accounts) towards third parties as well as to satisfy their tax obligations. How much of a part compilation plays in the total rendering of account by SMEs is dependent on the audit regime per country and the boundaries of the statutory audit.

So, for Horizontal Monitoring purposes, it matters whether we are talking about an audit or a compilation. With a compilation, it makes a difference here whether or not the SME is assisted by an intermediary. In particular, this revolves around the aspect of completeness of the revenue recognition. Despite the fact that an intermediary makes no representation concerning the completeness of the revenue recognition in a compilation, the involvement of the professional increases the reliability of the accountability. That will be particularly so if the intermediary is a professional who is personally subject to monitoring in the exercise of his profession.

The situation in the Netherlands is that this monitoring is in place not just for the professional (auditor), but also – in the context of the audit – for the audit firms. With respect to the compilation, indirect statutory monitoring is performed via the professional bodies, NBA and SRA. For the professional tax intermediary, monitoring is carried out via private-law organisations.

Techniques and technology

From the point of view of managing societal costs, it may be important that more added value is attached to a compilation by intermediaries in terms of the completeness of the revenue recognition and, derived from this, the completeness of tax revenue. Digitisation and big data, in particular, may play a part in achieving this. Application of this technology will make benchmarking accessible. This, linked to a good risk analysis, presents an even more reliable accountability mechanism for small entities, too, including as regards the aspect of completeness of the revenue recognition.

Zooming in on the Dutch situation: SRA, the organisation that I chair, already has a database of more than 140,000 annual financial statements, all from SMEs. More than half of the 360 members, audit firms, use this database in their compilation. The Dutch Tax and Customs Administration has also assessed our database and – I can safely say – is enthusiastic about the quality of the benchmarks that can be performed with it. They find that it adds value to get a good idea of the completeness of the revenue recognition for the compilation as well.

Within the framework of the development of Horizontal Monitoring, it is necessary to make a distinction between a compilation performed by a monitored third party and a compilation drawn up by the entrepreneur personally or by a third party that is not monitored. The techniques used also matter, such as benchmarking, validated software (ISA 3402 opinions), validated cash registers, and so on. This may lead to an audit for small entities that reduces the compilation element of the total rendering of account by businesses.

This then in economic terms may also lead to a potentially even better performance of the economy, especially for SMEs, as well as to a reduction in the checks required of the Tax and Customs Administration.

As a final point, I would also like to put the following to you: where an audit (validation) of annual accountability is currently the order of the day, the new techniques based on far-reaching



digitisation, such as continuous reporting for SMEs as well, may lead to a shift from assessment-based taxes to return-based taxes. Take the tax on profits, for example. SMEs will make more use of these techniques themselves to give them quicker access to reliable information. The entrepreneur sees the need for quicker information because the life cycle of business plans is becoming shorter and shorter due to the rapidly changing environment. It is a small step then to settle the tax on profits at intervals smaller than one year. This will improve the quality of the tax streams for the government. Of course, this will also impact on the setup of the monitoring (checks) by the Tax and Customs Administration. What kind of impact is still unclear.

Conclusion and summary

I will close now by saying that, in my opinion, in the near future SMEs will meet their tax obligations with validated statements. This can be achieved through better and increased application of digital information and big data. The next step is also to make the content of Horizontal Monitoring more professional. That is a task for the intermediary and the Tax and Customs Administration. The Tax and Customs Administration will also have to make a distinction as to what added value the intermediary delivers. The basis for this is a clear difference in the quality of the statements and the techniques used, and the way in which the aspect of completeness of the revenue recognition is achieved. The main stipulation here is that the entrepreneur engages a professional intermediary accredited for Horizontal Monitoring.

The need for a tax audit will remain, but the tax audit will be performed in a different manner. If an enterprise is subject to HM, there will be a shift towards an audit by firms accredited for HM. This will lead to lower audit costs and greater security for the entrepreneurs involved when it comes to complying with laws and regulations. Of course, the same is true of the government. The Tax and Customs Administration can then target its checks more at those enterprises that are not subject to HM. What is more, the effectiveness of these checks will increase significantly as the number of enterprises that are checked annually will also increase significantly – even exponentially.

Ladies and gentlemen,

I hope I have given you an insight into my view of the developments and the future of the audit and, more specifically, the tax audit. Thank you for giving me your attention.