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## Organization of the Internal Audit System at the Oil and Gas Company

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### Abstract:

The research subject of the article is the internal audit as one of the ways to control efficiency of oil and gas company activity. The aim of the study is to organize the internal audit of taxes and levies of the oil and gas company. Based on the summary program of company audit it is proposed to design the financial audit of taxes and levies. The program of audit on taxes and levies is drawn up in the form of an action pack. Practical approval of the proposed program allowed revealing a need to implement tax design. The author suggests recommended practice for the consistent implementation of the tax design through eight consolidated procedures and proposes tax management scheme for the oil and gas company. The calculations have shown that the implementation of tax coordination allows achieving significant savings of financial resources of the oil and gas company. Based on results obtained the author believes that the proposed system of internal audit of taxes and levies may serve a recommended practice for financial savings of oil and gas companies of the Russian Federation.

**Keywords:** oil and gas company, internal audit, tax design, tax coordinator.

**JEL Classification:** M21, H25, L95, M42.

### Introduction

The internal audit is one of the ways to control the company performance efficiency. Organization, role and functions of internal audit are defined by the company itself depending on the content and specificity of corporate activities, the level of its financial and economic performance indicators as well as the current management system and the status of internal control.

#### 1. Internal audit in oil and gas industry

The function of internal audit can be performed by special services or the separate auditors from the company staff, the auditing committees engaged for the purpose of internal audit as well as the third parties and the external auditors. Besides, internal audit has information and consulting value to the corporate top management. It is designed to assist in optimization of corporate activities and the responsibilities of its top management.

The objects of internal audit vary depending on the peculiarities of oil and gas company performance and the requirements of its management. Internal audit should be implemented for the following purposes:

- examination of accounting systems and internal control as well as development of recommendations for improving these systems;
- examination of accounting and operational information used for the assessment and classification of such information and preparation of financial statements on its basis as well as performance of detailed examination of the facts related to business functions and accounting balances;
- verification of laws and other normative acts as well as requirements of tax and accounting policy, instructions, managerial decisions and instructions;
- verification of availability, condition and security of company assets;
- evaluation of the software used by the company;
- development and submission of proposals on elimination of the revealed financial misconducts and errors as well as recommendations for improving the performance of oil and gas company.

The internal audit can be conducted in relation both to the entire company or its specific departments as well as with regard to certain documentation.

Objectivity of the internal audit is ensured by its independence within the corporate management structure, therefore, one of the accountants and economists should be charged with the responsibility of auditor to conduct an internal audit. Note that the purpose of the oil and gas company should consist in creation of a system that would help company to promptly identify and correct detected deviations, errors and inefficiencies, helping to improve corporate performance efficiency rather than creation of a monitoring system that would fully guarantee the lack of noted shortcomings. The internal audit system helps to adjust the corporate activities and individual company departments, allows establishing particular services and units of the company as well as lines of their activities that contribute to the achievement of the planned objectives and enhancement of the corporate performance.

The internal auditing is the assessment of the reliability and efficiency of the existing internal control system, while internal auditors are people qualified to conduct such assessments professionally and impartially. In other words, internal auditing is an independent assessment of all aspects of the corporate activities carried out in the company and focused on creation of conviction in the corporate management that the existing control system is reliable and efficient.

## 2. Action pack: carrying out verification on taxes and levies at the oil and gas company

It is proposed to plan financial audit on taxes and levies on the basis of the summary of corporate audit program presented in the form of an action pack and developed based on normative legal documents (Table 1).

**Table 1.** Action pack: carrying out verification on taxes and levies at the oil and gas company

The list of actions	Time frame	Auditor's schedule
1	2	3
1. Federal taxes audit	During the year	
1.1 VAT audit: <ul style="list-style-type: none"> <li>▪ establishing the terms of tax payment;</li> <li>▪ verification of the possibility of applying reliefs;</li> <li>▪ verification of taxable base formation;</li> <li>▪ verification the validity of deductions;</li> <li>▪ verification of the declaration accuracy and timeliness;</li> <li>▪ verification of accuracy of accrual and duly payment of taxes</li> </ul>	On due dates for tax payment	Accounting records, purchases and sales books, logs, invoices, payment orders, bank statements, and VAT returns
1.2 Audit of accounts on personal income tax: <ul style="list-style-type: none"> <li>▪ verification of taxable base formation;</li> <li>▪ verification the validity of deductions;</li> <li>▪ verification of the declaration accuracy and timeliness;</li> </ul>	On due dates for tax payment	Accounting records, record cards on personal income tax, payroll register, pay orders, bank statements, and VAT returns



to calculation and payment of taxes were primarily adjusted in accordance with the Tax Code of the Russian Federation.

The amendments that were introduced to the tax code during the reporting period did not affect the tax base.

Table 2 presents the accrual and payment of taxes and levies, penalties and fines in the reporting period.

**Table 2.** The accrual and payment of taxes and levies, penalties and fines, mln. rubles

Indicators	Accrued	Total	Paid Including restructured debt	Percentage paid (col.3/col.2)
Taxes and levies	1567.7	1624.7	0.2	103.7
Penalties and fines	1.3	2.3	-	176.9
Nontax payments	12.3	14.4	-	117.1
Penalties and fines on nontax payments	-0.1	0	-	-
<b>Total</b>	<b>1581.2</b>	<b>1641.4</b>	<b>0.2</b>	<b>103.8</b>
including:			-	
Federal	1414.2	1427.1	-	100.9
Regional	0.9	0.3	-	33.3
Local	6.3	6.1	0.2	96.8

At the beginning of 2014 the uncollected taxes and non-tax payments amounted to 86.6 mln. rubles, and taking into account accrued penalties and fines – to 87.2 mln. rubles. At the end of the year arrears inclusive of penalties and fines amounted to 33.6 mln. rubles. Reducing arrears on taxes is attributable to the reduction (2.6-fold) of taxable profits in Q4 compared to Q3 2014.

**Table 3.** The dynamics of the oil and gas company tax arrears, mln. rubles

Budgets	Balance as of 1.01.2013	Balance as of 1.01.2014	Variance
<b>Total</b>	<b>87.2</b>	<b>33.6</b>	<b>-53.6</b>
including			
Tax payments	85.1	32.4	-52.7
Taxes	84.5	33.9	-50.6
Penalties and fines	0.6	-1.5	-2.1
Federal	87.3	76	-11.3
Taxes	87.7	75.8	-11.9
Penalties and fines	-0.4	0.2	0.6
Regional	0.5	-0.9	-1.4
Taxes	0.5	-0.9	-1.4
Local	-2.7	-2.7	0
Taxes	-3.0	-2.6	0.4
Penalties	0.3	-0.1	-0.4

Budgets	Balance as of 1.01.2013	Balance as of 1.01.2014	Variance
Non-tax payments	2.1	1.2	-0.9
Federal	1.9	0.7	-1.2
Regional	0	-0.2	-0.2
Local	0.2	-0.3	-0.5

In accordance with the procedure determining the tax burden of economic entity, at the level of tax burden within the range of 20-35%, it is advisable for company to have tax design coordinator.

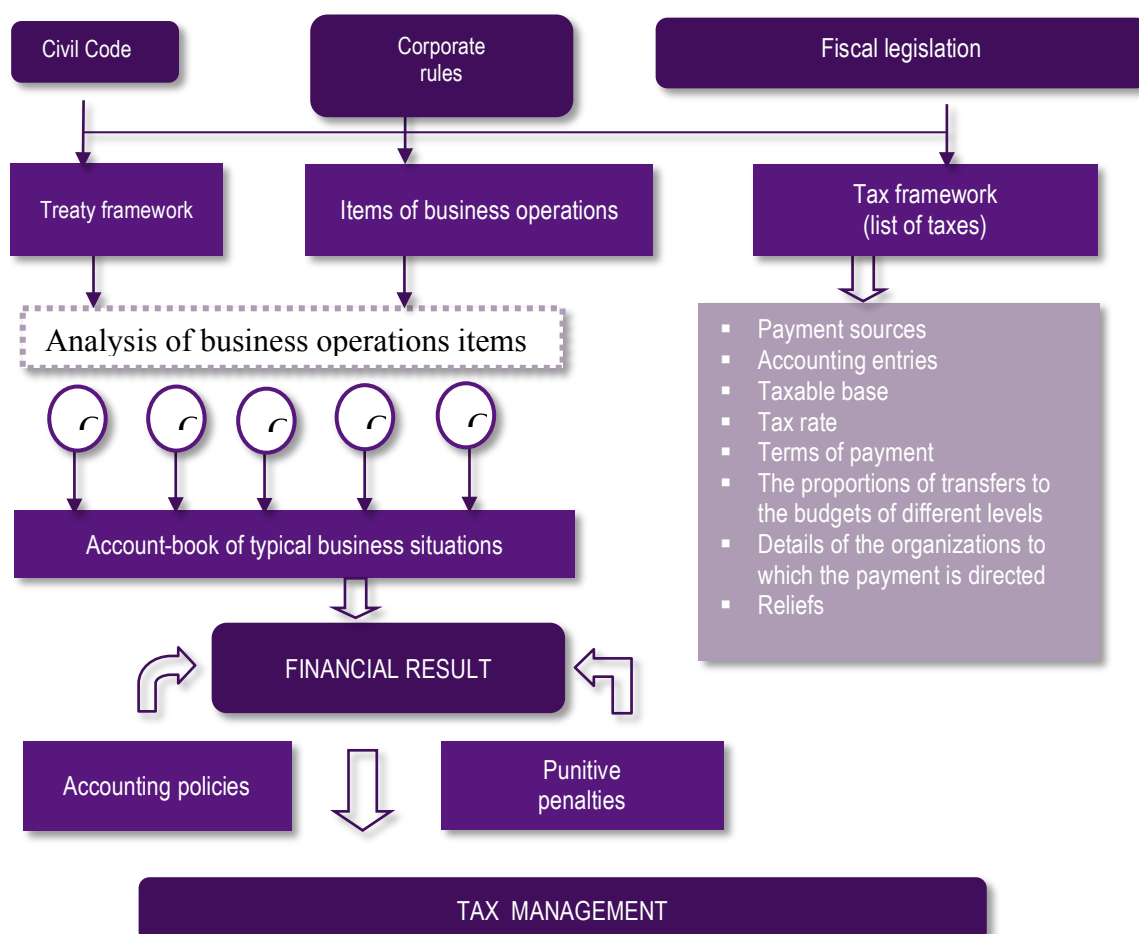


Figure 1. The diagram of the current tax design in the oil and gas company

In the first stage of tax design in the oil and gas company tax coordinator draws out a general framework of the current tax design (Figure 1), where 'C' are different situations with regard to tax, contractual and economic practices made by company specialists. The sequence of tax design consists of eight integrated procedures.

- (1) In accordance with the corporate status and based on its charter and legislative acts in the field of taxation tax coordinator determines the range of the main taxes and fees which must be paid to the budget and extra-budgetary funds. He draws up a tax table, which describes the tax framework of the oil and gas company. Then, tax coordinator analyzes all the reliefs provided by legislation for each of the taxes and levies with respect to their practical use. Based on the results of this analysis, tax coordinator prepares a detailed plan for the use of reliefs on selected payments. Reduction in the tax burden is connected primarily to a full use of the entire set of tax reliefs offered by the Russian legislation. Typically, economists and accountants to the full extent are not using a significant portion of these reliefs. One reason for this is the intangible idea about the overall tax relief system and the application procedure for certain taxes.

- (2) According to the corporate charter and based on the civil law, the company forms contractual relations (contractual framework). In the framework of the current activity company plans possible forms of bargains: lease, contract, purchase and sale. Each bargain must be assessed from the viewpoint of possible tax consequences at the time of preparation of documents, *i.e.* before the bargain becomes legally concluded.
- (3) The typical facts of economic activities that should be implemented by the company come under review.
- (4) Different scenarios are developed taking into account tax, contract and economic practices.
- (5) The best options are determined that should be recorded in the form of accounting entries and/or tax transactions and models.
- (6) The appropriate blocks are used to compose the account-book of typical business situations. This account-book serves the basis for conducting financial and tax accounting.
- (7) Tax coordinator estimates the capabilities for obtaining the maximum financial result with due account for tax risks (possible punitive penalties) and allocates company assets and financial results in the most rational way in terms of a tax perspective.
- (8) The alternative methods for corporate accounting and tax policies are defined.

In accordance with the basic framework of the tax optimization, tax coordinator develops a tax management program for oil and gas company (Figure 2) in a form of action pack consisting of four stages.

Greater importance should be given to tax computations and primarily to exception of arithmetic and accounting errors. The internal control technology of the tax computations may be primary way to reduce the risk of errors.

This technology allows eliminating the subjectivity in making tax decisions. For this purpose tax coordinator develops documents and paperwork, technological workflow and models as well as the procedures for their implementation.

The tax design in the oil and gas company is also based on the strict control over the due dates for tax payment. With this purpose, tax coordinator forms tax calendar, which besides the dates of tax payment specifies the grounds on which tax is charged and establishes the responsibility for violation of tax legislation.

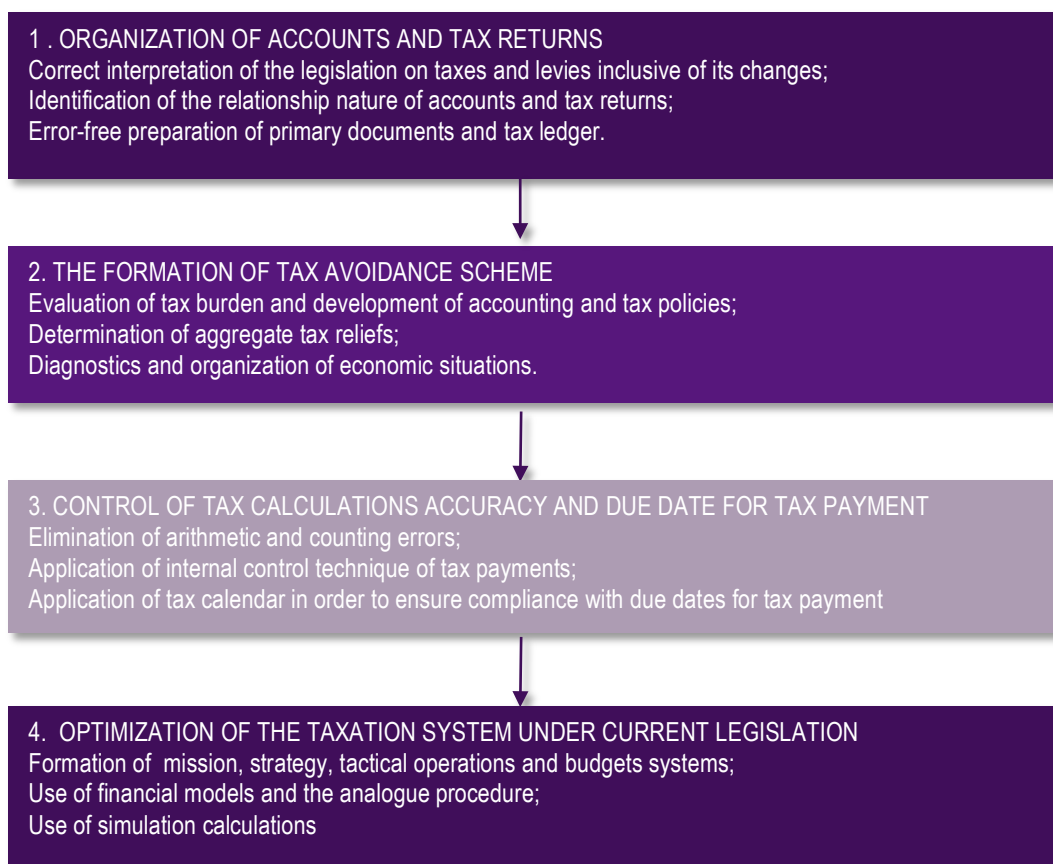


Figure 2. Action pack: tax management of the oil and gas company

In accordance with Table 2, penalties and fines on tax payments of the oil and gas company amount to 1.3 mln rubles. Thus, savings from the implementation of a tax design may amount to 975,000 rubles.

### Conclusion

Based on the results obtained we believe that the proposed system of internal audit of taxes and levies may serve a recommended practice for financial savings of oil and gas companies of the Russian Federation.

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