

Part III. Administrative, Procedural, and Miscellaneous

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Required Records Author: Institutional
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Guidance Offered On Electronic Records

The Service has provided guidance (Rev. Proc. 97-22) for taxpayers that use an electronic storage system to maintain their books and records.

===== SUMMARY =====

The Service has provided guidance (Rev. Proc. 97-22) for taxpayers that use an electronic storage system to maintain their books and records. Records in an electronic storage system that complies with Rev. Proc. 97-22 will be records within the meaning of section 6001.

The guidance defines an electronic storage system as one to prepare, record, transfer, index, store, preserve, retrieve, and reproduce books and records by either electronically imaging hardcopy documents to an electronic storage media, or transferring computerized books and records to an electronic storage media that allows them to be viewed or reproduced without using the original program.

Rev. Proc. 97-22 permits the destruction of the original hardcopy books and records and the deletion of original computerized records after a taxpayer completes testing of the storage system to establish that books and records can be reproduced in compliance with Rev. Proc. 97-22 and institutes procedures to ensure continued compliance. The district director may issue a Notice of Inadequate Records under reg. Section 1.6001-1(d) if a taxpayer's books and records are only available electronically and the system fails the requirements of the revenue procedure.

===== FULL TEXT =====

26 CFR 601.105 Examination of returns and claims for refund, credits or abatement; determination of correct tax liability. (Also Part I, Section 6001; 1.6001-1.)

Rev. Proc. 97-22

SECTION 1. PURPOSE

This revenue procedure provides guidance to taxpayers that maintain books and records by using an electronic storage system that either images their hardcopy (paper) books and records, or transfers their computerized books and records, to an electronic storage media, such as an optical disk. Records maintained in an electronic storage system that complies with the requirements of this revenue procedure will constitute records within the meaning of section 6001 of the Internal Revenue Code.

SECTION 2. BACKGROUND

.01 Section 6001 provides that every person liable for any tax imposed by the Code, or for the collection thereof, must keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever necessary, the Secretary may require any person, by notice served upon that person or by regulations, to make such returns, render such statements, or keep such records, as the Secretary deems sufficient to show whether or not that person is liable for tax.

.02 Section 1.6001-1(a) of the Income Tax Regulations provides that, except for farmers and wage-earners, any person subject to income tax, or any person required to file a return of information with respect to income, must keep such books and records, including inventories, as are sufficient to establish the amount of gross income, deductions, credits, or other matters required to be shown by that person in any return of such tax or information.

.03 Section 1.6001-1(e) provides that the books or records required by section 6001 must be kept available at all times for inspection by authorized internal revenue officers or employees, and must be retained so long as the contents thereof may become material in the administration of any internal revenue law.

SECTION 3. SCOPE

.01 This revenue procedure applies to taxpayers who maintain books and records using an "electronic storage system." An electronic storage system

is a system to prepare, record, transfer, index, store, preserve, retrieve, and reproduce books and records by either:

(1) electronically imaging hardcopy documents to an electronic storage media; or

(2) transferring computerized books and records to an electronic storage media using a technique such as "COLD" (computer output to laser disk), which allows books and records to be viewed or reproduced without the use of the original program.

.02 The requirements of this revenue procedure pertain to all matters under the jurisdiction of the Commissioner of Internal Revenue including, but not limited to, income, excise, employment, and estate and gift taxes, as well as employee plans and exempt organizations.

.03 A taxpayer's use of a third party (such as a service bureau or time-sharing service) to provide the taxpayer with an electronic storage system for its books and records does not relieve the taxpayer of the responsibilities described in this revenue procedure.

.04 Except as otherwise provided in this revenue procedure, all requirements of section 6001 that apply to hardcopy books and records apply as well to books and records that are stored electronically pursuant to this revenue procedure.

SECTION 4. ELECTRONIC STORAGE SYSTEM REQUIREMENTS

.01 General Requirements.

(1) An electronic storage system must ensure an accurate and complete transfer of the hardcopy or computerized books and records to an electronic storage media. The electronic storage system must also index, store, preserve, retrieve, and reproduce the electronically stored books and records.

(2) An electronic storage system must include:

(a) reasonable controls to ensure the integrity, accuracy, and reliability of the electronic storage system;

(b) reasonable controls to prevent and detect the unauthorized creation

of, addition to, alteration of, deletion of, or deterioration of electronically stored books and records;

(c) an inspection and quality assurance program evidenced by regular evaluations of the electronic storage system including periodic checks of electronically stored books and records;

(d) a retrieval system that includes an indexing system (within the meaning of section 4.02 of this revenue procedure); and

(e) the ability to reproduce legible and readable hardcopies (within the meaning of section 4.01(3) of this revenue procedure) of electronically stored books and records.

(3) All books and records reproduced by the electronic storage system must exhibit a high degree of legibility and readability when displayed on a video display terminal and when reproduced in hardcopy. The term "legibility" means the observer must be able to identify all letters and numerals positively and quickly to the exclusion of all other letters or numerals. The term "readability" means that the observer must be able to recognize a group of letters or numerals as words or complete numbers. The taxpayer must ensure that the reproduction process maintains the legibility and readability of the electronically stored document.

(4) The information maintained in an electronic storage system must provide support for the taxpayer's books and records (including books and records in an automated data processing system). For example, the information maintained in an electronic storage system and the taxpayer's books and records must be cross-referenced in a manner that provides an audit trail between the general ledger and the source document(s).

(5) For each electronic storage system used, the taxpayer must maintain, and make available to the Service upon request, complete descriptions of:

(a) the electronic storage system, including all procedures relating to its use; and

(b) the indexing system (see section 4.02 of this revenue procedure).

(6) At the time of an examination, or for the tests described in section 5 of this revenue procedure, the taxpayer must:

(a) retrieve and reproduce (including hardcopies if requested) electronically stored books and records; and

(b) provide the Service with the resources (e.g., appropriate hardware and software, personnel, documentation, etc.) necessary to locate, retrieve, read, and reproduce (including hardcopies) any electronically stored books and records.

(7) An electronic storage system must not be subject, in whole or in part, to any agreement (such as a contract or license) that would limit or restrict the Service's access to and use of the electronic storage system on the taxpayer's premises (or any other place where the electronic storage system is maintained), including personnel, hardware, software, files, indexes, and software documentation.

(8) The taxpayer must retain electronically stored books and records so long as their contents may become material in the administration of the Internal Revenue laws under section 1.6001- 1(e).

(9) The taxpayer may use more than one electronic storage system. In that event, each electronic storage system must meet the requirements of this revenue procedure. Electronically stored books and records that are contained in an electronic storage system with respect to which the taxpayer ceases to maintain the hardware and the software necessary to satisfy the conditions of this revenue procedure will be deemed destroyed by the taxpayer, unless the electronically stored books and records remain available to the Service in conformity with this revenue procedure.

(10) Taxpayers may use reasonable data compression or formatting technologies as part of their electronic storage system so long as the requirements of this revenue procedure are satisfied.

.02 Requirements of an Indexing System.

(1) For purposes of this revenue procedure, an "indexing system" is a system that permits the identification and retrieval for viewing or

reproducing of relevant books and records maintained in an electronic storage system. For example, an indexing system might consist of assigning each electronically stored document a unique identification number and maintaining a separate database that contains descriptions of all electronically stored books and records along with their identification numbers. In addition, any system used to maintain, organize, or coordinate multiple electronic storage systems is treated as an indexing system under this revenue procedure. The requirement to maintain an indexing system will be satisfied if the indexing system is functionally comparable to a reasonable hardcopy filing system. The requirement to maintain an indexing system does not require that a separate electronically stored books and records description database be maintained if comparable results can be achieved without a separate description database.

(2) Reasonable controls must be undertaken to protect the indexing system against the unauthorized creation of, addition to, alteration of, deletion of, or deterioration of any entries.

.03 Recommended Practices. The implementation of records management practices is a business decision that is solely within the discretion of the taxpayer. Records management practices may include the labeling of electronically stored books and records, providing a secure storage environment, creating back-up copies, selecting an off-site storage location, retaining hardcopies of books or records that are illegible or that cannot be accurately or completely transferred to an electronic storage system, and testing to confirm records integrity.

SECTION 5. DISTRICT DIRECTOR TESTING

.01 The District Director may periodically initiate tests of a taxpayer's electronic storage system. These tests may include an evaluation (by actual use) of a taxpayer's equipment and software, as well as the procedures used by a taxpayer to prepare, record, transfer, index, store, preserve, retrieve, and reproduce electronically stored documents. In some instances, the District Director may choose to review the internal controls, security procedures, and documentation

associated with the taxpayer's electronic storage system.

.02 The tests described in section 5.01 of this revenue procedure are not an "examination," "investigation," or "inspection" of the books and records within the meaning of section 7605(b), or a prior audit for purposes of section 530 of the Revenue Act of 1978, 1978-3 (Vol.1) C.B. 119, as amended by section 1122 of the Small Business Job Protection Act of 1996, because these tests are not directly related to the determination of the tax liability of a taxpayer for a particular taxable period.

.03 The District Director must inform the taxpayer of the results of any tests under this section.

SECTION 6. COMPLIANCE

.01 A taxpayer's electronic storage system that meets the requirements of this revenue procedure will be treated as being in compliance with the recordkeeping requirements of section 6001 and the regulations thereunder.

.02 A taxpayer's electronic storage system that fails to meet the requirements of this revenue procedure may be treated as not being in compliance with the recordkeeping requirements of section 6001 and the regulations thereunder. See section 9 of this revenue procedure for applicable penalties. However, even though a taxpayer's electronic storage system fails to meet the requirements of this revenue procedure, the penalties described in section 9 of this revenue procedure may not apply if the taxpayer maintains its original books and records, or maintains its books and records in micrographic form in conformity with Rev. Proc. 81-46, 1981-2 C.B. 621.

SECTION 7. DESTRUCTION AND DELETION OF ORIGINAL BOOKS AND RECORDS

This revenue procedure permits the destruction of the original hardcopy books and records and the deletion of the original computerized records (other than "machine-sensible" records required to be retained by Rev. Proc. 91-59, 1991-2 C.B. 841), after the taxpayer:

(1) has completed its own testing of the electronic storage system that establishes that hardcopy or computerized books and records are being reproduced in compliance with all the provisions of this revenue procedure; and

(2) has instituted procedures that ensure its continued compliance with all the provisions of this revenue procedure.

SECTION 8. IMPACT ON MACHINE-SENSIBLE RECORDS

The provisions of this revenue procedure regarding electronically stored books and records do not relieve taxpayers of the responsibility of retaining any other books and records required to be retained under section 6001. Such other books and records may include "machine-sensible" records required to be retained by Rev. Proc. 91-59 in connection with the taxpayer's use of an automatic data processing (ADP) system.

SECTION 9. PENALTIES

The District Director may issue a Notice of Inadequate Records pursuant to section 1.6001-1(d) if the taxpayer's books and records are available only as electronically stored books and records and the taxpayer's electronic storage system fails to meet the requirements of this revenue procedure. Taxpayers whose electronic storage system fails to meet the requirements of this revenue procedure may also be subject to applicable penalties under subtitle F of the Code, including the section 6662(a) accuracy-related civil penalty and the section 7203 willful failure criminal penalty.

SECTION 10. INTERNAL REVENUE SERVICE OFFICE CONTACT

.01 Questions regarding this revenue procedure should be directed to the Office of the Assistant Commissioner (Examination). The telephone number for this office is (202)622-5480 (not a toll-free number). Written questions should be addressed to:

Assistant Commissioner
(Examination) Attention: CP:EX
Internal Revenue
Service 1111 Constitution Ave., N.W.
Washington, D.C. 20224

.02 Questions regarding the application of this revenue procedure to a specific factual situation should be directed to the appropriate District Director.

SECTION 11. PAPERWORK REDUCTION ACT

The collections of information contained in this revenue procedure have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1533.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

The collections of information are in sections 4 and 5 of this revenue procedure. This information is required to ensure that records maintained in an electronic storage system will constitute records within the meaning of section 6001. The collections of information are mandatory for a taxpayer who chooses to electronically store its books and records. The likely respondents are individuals, state or local governments, farms, business or other for-profit institutions, federal agencies or employees, nonprofit institutions, and small businesses or organizations.

The estimated total annual recordkeeping burden is 1,000,400 hours.

The estimated annual burden per recordkeeper will vary from 20 hours to 22 hours, depending on individual circumstances, with an estimated average of 20 hours. The estimated number of recordkeepers is 50,000.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

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