

Japan Tax Bulletin

Tax Reform on the Electronic Preservation System for Books and Documents

September 2023

The electronic preservation system for books and documents is a system for storing books, receipts, invoices, financial statements, and other national tax-related documents that are required to be preserved under tax law in electronic data format instead of paper format, and is divided into the following three categories. The system is stipulated in “the Act on Special Provisions concerning Preservation Methods for Books and Documents Related to National Tax Prepared by Means of Computers” (“the Act”).

1. *Electronic Preservation for Books and Documents*

Books of account and national tax-related documents prepared on a computer, etc. can be preserved as electronic data, instead of being printed out and preserved. Furthermore, if a certain range of books of account is preserved in electronic data by meeting the requirements for “excellent” electronic books there is a measure that reduces the additional tax on underreporting by 5% (10%→5%) even if an underreporting related to such electronic books of account is later discovered. In order to be eligible for this exemption, a notification must be submitted in advance.

2. *Scanner preservation*

Paper receipts, invoices, and other documents received from business partners can be saved as electronic data scanned with a smartphone or scanner, instead of saving the documents themselves.

3. *Electronic transactions*

If those who are subject to the obligation to preserve books and documents with respect to individual income tax and corporate tax, receive electronic data such as purchase orders, contracts, invoices, receipts, estimates, invoices, etc., they must preserve them as electronic data.

The overview of these systems has already been explained in our tax bulletin of September 2021, and the following three revisions were made in the 2023 tax reform:

- A) Change in the scope of “excellent” electronic books
- B) Relaxed requirements for scanner preservation system
- C) Revision of the requirements for preservation of electronic transaction

A) *Change in the scope of “excellent” electronic books*

If there is an omission in a tax return with respect to matters recorded in national tax-related books, an additional tax for underreporting will be imposed on the omission. However, if the

books of account meet the requirements of “excellent” electronic books, the additional tax on underreporting will be reduced by 5%.

Under the tax reform, the scope of books that must be prepared as electronic books to qualify for the “excellent” electronic books requirement has been revised as follows for both individual income tax and corporate tax. The scope has been clearly limited.

Before the revision.

- (1) Journal ledger;
- (2) General ledger; and
- (3) All other required ledgers.

After the revision.

Limited to the following entries:

- (1) Journal ledger;
- (2) General ledger; and
- (3) Books other than 1. and 2. pertaining to the following entries:
 - Bills
 - Accounts receivable, etc.
 - Accounts payable, etc.
 - Marketable securities
 - Depreciable assets
 - Deferred assets
 - Sales and other income
 - Purchases and other expenses

There is no change in the scope of books that must be prepared as “excellent” electronic books for consumption tax purposes.

This tax reform will be applied to national tax returns due on or after January 1, 2024.

B) *Relaxed Requirements for Scanner Preservation*

The requirements for scanner preservation were eased in the 2022 tax reform, and the following three points will be further reviewed this time. It can be said that the work man-hours for scanner preservation has been reduced, making it easier to use the scanner preservation system.

a) *Abolition of the requirement to preserve information on resolution, tone and size*

The requirement to preserve information on the resolution, tone, and size of tax-related documents scanned by scanners has been abolished. Although it is no longer necessary to retain this information, the requirements for resolution (200dpi or higher) and tone (color images in principle) that must be maintained when scanning remain unchanged.

b) Abolition of the requirement to confirm information on the person who entered the recorded items, etc.

The requirement to be able to verify information regarding the person who enters recorded matters or the person who directly supervises such person at the time of scanner storage has been eliminated. The same applies to electronic transactions.

c) Documents that must be able to confirm interrelationships are limited to important documents such as contracts and receipts.

National tax-related documents that need to be scanned so that their relationship to the ledger can be confirmed are now limited to "important documents such as documents that are directly linked to the flow of funds or goods, such as contracts, receipts, invoices, delivery slips, etc.". As a result of this reform, it is no longer necessary to ensure interrelationships when scanning and storing general documents such as documents that are not directly linked to the flow of funds or goods, such as quotations, order forms, etc., and copies of delivery receipts.

This tax reform will be applied to national tax-related documents to be preserved on and after January 1, 2024.

C) Revision of preservation requirements for electronic transactions

The preservation requirements for electronic transactions have also been revised as follows

a) The following are the revised targets for which all of the search requirements are no longer required.

The requirement for persons obliged to preserve the data has been limited from persons whose sales for the base period were JPY10 million or less to persons whose sales for the base period were JPY50 million or less.

In addition, "persons obligated to preserve electronic transaction data that are capable of presenting or submitting printed documents of electronic transaction data, organized by transaction date or other date and by counterparty" have been added to the targets for which all of the search requirements are no longer required.

This tax reform not only raises the upper limit on the size of companies eligible for the exemption, but also significantly eases the exemption for any company that is able to present or submit the output document.

b) Abolition of the requirement to confirm information regarding the person who preserves electromagnetic records, etc.

There are two major requirements for the preservation of electronic transactions: the "truthfulness requirement" and the "visibility requirement".

One of the "truthfulness requirements" was to promptly time-

stamp the transaction information after it has been exchanged, and to make it possible to verify information regarding the person who preserves or supervises the preservation of the information. However, under the recent tax reform, the "information regarding the person who preserves or supervises the preservation" part is no longer required.

c) Institutionalization of "appeasement measures" in the mandatory preservation of electromagnetic records

The mandatory electronic preservation of electromagnetic records (abolition of measures for preservation by means of electronic data output documents, etc.) was the content included in the tax reform of the Act in 2022. However, the preparation period leading up to the enforcement of the revised law was short, and many companies were still not able to comply with the law even at the last minute. In light of this situation, in December 2021, just prior to the enforcement of the revised law, "appeasement measures" were established in the 2022 tax reform.

Specifically, electromagnetic records may be saved as paper output for two years until 2024 under the following two conditions: "under unavoidable circumstances" and "when the request for downloading, presentation or submission of the output document is accepted". The measure also stated that electronic storage would be mandatory after 2024, as it was originally intended.

This "appeasement measure" will be abolished as of December 31, 2023, but a new permanent grace measure was established by the 2023 reform.

Under the grace measure, if both of the following requirements (a) and (b) are met, it is no longer necessary to follow the requirements that must be met at the time of storage, such as tamper-prevention and search functions, and the electronic transaction data can simply be stored.

- (a) Where the head of the competent tax office finds reasonable cause for failing to preserve the electronic transaction data in accordance with the requirements to be met at the time of preservation.
- (b) Where the taxpayer is able to respond to a request to download the electronic transaction data and a request to present or submit a document containing a printout of the electronic transaction data at the time of a tax audit, etc.

No prior application is required for this grace measure.

These tax reforms will apply to electronic transactions conducted on and after January 1, 2024.