

THIS PROPOSED RULE IS SUBMITTED FOR PUBLIC COMMENTS AFTER INPUT FROM INTERESTED PARTIES AND IS TO BE USED SOLELY FOR DISCUSSION PURPOSES AT THE PUBLIC HEARING ON THE PROPOSED RULE. UNDER NO CIRCUMSTANCES IS THIS PROPOSED RULE TO BE USED TO DETERMINE TAX LIABILITY AND OR EXEMPTIONS.

AMENDATORY SECTION (Amending Order 89-6, filed 5/16/89)

WAC 458-20-254 Recordkeeping. (~~(1) Every person liable for an excise tax imposed by the laws of the state of Washington for which the department of revenue has primary or secondary administrative responsibility, i.e., Title 82 RCW, and, chapters 67.28 (hotel/motel tax), 70.93 (litter tax), 70.95 (tax on tires), and 84.33 RCW (forest excise tax), shall keep complete and adequate records from which the department may determine any tax for which such person may be liable.~~

~~(2) **General requirements.**~~

~~(a) It is the duty of each taxpayer to prepare and preserve all books of record in a systematic manner conforming to accepted accounting methods and procedures. Records are to be kept, preserved, and presented upon request of the department which will demonstrate:~~

~~(i) The amounts of gross receipts and sales from all sources, however derived, including barter or exchange transactions, whether or not such receipts or sales are taxable. These amounts must be supported by original source documents including but not limited to all purchase and sales invoices and contracts or such other documents as may be necessary to substantiate gross receipts and sales;~~

~~(ii) The amounts of all deductions, exemptions, or credits claimed through supporting documentation required by statute or administrative rule, or such other supporting documentation necessary to substantiate the deduction, exemption, or credit.~~

~~(b) The records kept, preserved and presented must include the normal books of account maintained by an ordinary prudent business person. Such records may include general ledgers, sales journals, cash receipts journals, check registers, and purchase journals, together with all bills, invoices, cash register tapes, or other documents of original entry supporting the books of account entries. The records shall include all federal and state tax returns and reports and all schedules or work papers used in the preparation of tax reports or returns.~~

~~(c) All such records shall be open for inspection and examination at any time by the department, upon reasonable notice, and shall be kept and preserved for a period of five years. RCW 82.32.070~~

~~(3) **Microfilm and/or microfiche.** Records may be~~

~~microfilmed or microfiched, such as general books of accounts including cash books, journals, voucher registers, ledgers and like documents provided the microfilmed and/or microfiched records are authentic, accessible, and readable, and all of the following requirements are fully satisfied:~~

~~(a) Appropriate facilities are provided to preserve the films or fiche for the periods such records are required to be open to examination and to provide transcriptions of any information on film or fiche required to verify tax liability.~~

~~(b) All microfilmed or microfiched data must be indexed, cross referenced, and labeled to show beginning and ending numbers and beginning and ending alphabetical listings of all documents included.~~

~~(c) Taxpayers must make available upon request of the department, a reader/printer in good working order at the examination site for reading, locating, and reproducing any record that is maintained on microfilm or microfiche.~~

~~(d) Taxpayers must set forth in writing the procedures governing the establishment of a microfilm or microfiche system and the names of persons who are responsible for maintaining and operating the system with appropriate authorization from the boards of directors, general partner(s), or owner(s), whichever is applicable.~~

~~(e) The microfilm or microfiche system must be complete and must be used consistently in the regularly conducted activity of the business.~~

~~(f) Taxpayers must establish procedures with the appropriate documentation so that an original document can be traced through the microfilm or microfiche system.~~

~~(g) Taxpayers must establish internal procedures for microfilm or microfiche inspection and quality assurance.~~

~~(h) Taxpayers must keep a record identifying where, when, by whom, and on what equipment the microfilm or microfiche was produced.~~

~~(i) When displayed on a microfilm or microfiche reader (viewer) or reproduced on paper, the material must be legible and readable. For this purpose, legible means the quality of a letter or numeral which enables the reader to identify it positively and quickly to the exclusion of all other letters or numerals. Readable means the quality of a group of letters or numerals recognizable as words or complete numbers.~~

~~(j) All production of microfilm or microfiche and the processing, duplication, quality control, storage, identification, and inspection thereof must meet industry standards as set forth by the American National Standards Institute, National Micrographics Association, or National Bureau of Standards.~~

~~(4) **Automated data process system.** An automated data process (ADP) accounting system may be used to provide the~~

~~records required to verify tax liability. All ADP systems used for this purpose must include a method for producing legible and readable records to verify tax liability, reporting, and payment. The following requirements apply to any taxpayer who maintains records on an ADP system:~~

~~(a) ADP records shall provide an opportunity to trace any transaction back to the original source or forward to a final total. If detailed printouts are not made of transactions at the time they are done, the system must have the capability to reconstruct these transactions.~~

~~(b) A general ledger, with source references, shall be written out to coincide with financial reports for tax reporting periods. In the cases where subsidiary ledgers are used to support the general ledger accounts, the subsidiary ledgers shall be written out periodically.~~

~~(c) The audit trail shall be so designed that the details underlying the summary accounting data may be identified and made available to the department and that supporting documents, such as sales invoices, purchase invoices, credit memoranda, and like documents are readily available.~~

~~(d) A description of the ADP portion of the accounting system shall be made available. The statements and illustrations as to the scope of operations shall be sufficiently detailed to indicate:~~

~~(i) The application being preformed;~~

~~(ii) The procedures employed in each application (which, for example, might be supported by flow charts, block diagrams or other satisfactory description of the input or output procedures); and,~~

~~(iii) The controls used to insure accurate and reliable processing.~~

~~(e) Important changes in an ADP accounting system or any part thereof, together with their effective dates, shall be noted to preserve an accurate chronological record of such changes.~~

~~(f) Adequate record retention facilities shall be available for the storage of such information, printouts and all supporting documents.~~

~~(5) **Out-of-state businesses.** An out-of-state business which does not keep the necessary records within this state may either produce within this state such records as are required for examination by the department, or, permit the examination of the records by the department at the place where the records are kept. RCW 82.32.070, see also, WAC 458-20-215.~~

~~(6) **Failure of taxpayer to maintain and disclose complete and adequate records.** Any person who fails to comply with the requirements of RCW 82.32.070 or this section shall be forever barred from questioning, in any court action or proceedings, the correctness of any assessment of taxes made by the department~~

~~based upon any period for which such books, records, and invoices have not been so kept and preserved. RCW 82.32.070)~~

(1) **Introduction.** This section defines the requirements for the maintenance and retention of books, records, and other sources of information. It also addresses these requirements where all or a part of the taxpayer's books and records are received, created, maintained, or generated through various computer, electronic, and/or imaging processes and systems.

(2) **Definitions.** For purposes of this section, the following definitions will apply:

(a) "Data base management system" means a software system that controls, relates, retrieves, and provides accessibility to data stored in a data base.

(b) "Electronic data interchange" or "EDI technology" means the computer-to-computer exchange of business transactions in a standardized structured electronic format.

(c) "Hard copy" means any documents, records, reports or other data printed on paper.

(d) "Machine-sensible record" means a collection of related information in any electronic format (e.g., data base management systems, EDI technology, automated data process systems, etc.). Machine-sensible records do not include hard-copy records that are created or recorded on paper or stored in or by an imaging system such as microfilm, microfiche, or storage-only imaging systems.

(e) "Records" means all books, data, documents, reports, or other information, including those received, created, maintained, or generated through various computer, electronic, and/or imaging processes and systems.

(f) "Storage-only imaging system" means a system of computer hardware and software that provides for the storage, retention and retrieval of documents originally created on paper. It does not include any system, or part of a system, that manipulates or processes any information or data contained on the document in any manner other than to reproduce the document in hard copy or as an optical image.

(3) **Recordkeeping requirements--General.**

(a) Every taxpayer liable for a tax or fee imposed by the laws of the state of Washington for which the department of revenue ("department") has primary or secondary administrative responsibility, e.g., Title 82 RCW, chapter 67.28 RCW (hotel/motel tax), chapter 70.95 RCW (fee on tires), and chapter 84.33 RCW (forest excise tax), must keep complete and adequate records from which the department may determine any tax liability for such taxpayer.

(b) It is the duty of each taxpayer to prepare and preserve all records in a systematic manner conforming to accepted accounting methods and procedures. Such records are to be kept, preserved, and presented upon request of the department or its

authorized representatives which will demonstrate:

(i) The amounts of gross receipts and sales from all sources, however derived, including barter or exchange transactions, whether or not such receipts or sales are taxable. These amounts must be supported by original source documents or records including but not limited to all purchase invoices, sales invoices, contracts, and such other records as may be necessary to substantiate gross receipts and sales.

(ii) The amounts of all deductions, exemptions, or credits claimed through supporting records or documentation required by statute or administrative rule, or other supporting records or documentation necessary to substantiate the deduction, exemption, or credit.

(iii) The payment of retail sales tax or use tax on capital assets, supplies, articles manufactured for your own use, and other items used by the taxpayer as a consumer.

(iv) The amounts of any refunds claimed. These amounts must be supported by records as may be necessary to substantiate the refunds claimed. Refer to WAC 458-20-229 for information on the refund process.

(c) The records kept, preserved, and presented must include the normal records maintained by an ordinary prudent business person. Such records may include general ledgers, sales journals, cash receipts journals, bank statements, check registers, and purchase journals, together with all bills, invoices, cash register tapes, and other records or documents of original entry supporting the books of account entries. The records must include all federal and state tax returns and reports and all schedules, work papers, instructions, and other data used in the preparation of the tax reports or returns.

(d) If a taxpayer retains records in both machine-sensible and hard-copy formats, the taxpayer must make the records available to the department in machine-sensible format upon request of the department. However, the taxpayer is not prohibited from demonstrating tax compliance with traditional hard-copy documents or reproductions thereof, although this does not eliminate the requirement that they provide access to machine-sensible records, if requested.

(e) Machine-sensible records used to establish tax compliance must contain sufficient transaction-level detail information so that the details underlying the machine-sensible records can be identified and made available to the department upon request.

(f) At the time of an examination, the retained records must be capable of being retrieved and converted to a readable record format, as required in subsection (6) of this section.

(g) Taxpayers are not required to construct machine-sensible records other than those created in the ordinary course of business. A taxpayer who does not create the electronic

equivalent of a traditional paper document in the ordinary course of business is not required to construct such a record for tax purposes.

(4) **Record retention period.** All records must be open for inspection and examination at any time by the department, upon reasonable notice, and must be kept and preserved for a period of five years. RCW 82.32.070

(5) **Failure to maintain or disclose records.** Any taxpayer who fails to comply with the requirements of RCW 82.32.070 or this section is forever barred from questioning, in any court action or proceedings, the correctness of any assessment of taxes made by the department based upon any period for which such books, records, and invoices have not been so kept, preserved, or disclosed. RCW 82.32.070

(6) **Electronic records.**

(a) **Electronic data interchange requirements.**

(i) Where a taxpayer uses electronic data interchange (EDI) processes and technology, the level of record detail, in combination with other records related to the transactions, must be equivalent to that contained in an acceptable paper record. For example, the retained records should contain such information as vendor name, invoice date, product description, quantity purchased, price, amount of tax, indication of tax status, shipping detail, etc. Codes may be used to identify some or all of the data elements, provided that the taxpayer provides a method which allows the department to interpret the coded information.

(ii) The taxpayer may capture the information at any level within the accounting system and need not retain the original EDI transaction records provided the audit trail, authenticity, and integrity of the retained records can be established. For example, a taxpayer using electronic data interchange technology receives electronic invoices from its suppliers. The taxpayer decides to retain the invoice data from completed and verified EDI transactions in its accounts payable system rather than to retain the EDI transactions themselves. Since neither the EDI transaction nor the accounts payable system captures information from the invoice pertaining to product description and vendor name (i.e., they contain only codes for that information), the taxpayer must also retain other records, such as its vendor master file and product code description lists and make them available to the department. In this example, the taxpayer need not retain its EDI transaction for tax purposes if the vendor master file contains the required information.

(b) **Electronic data processing systems requirements.** The requirements for an electronic data processing accounting system should be similar to that of a manual accounting system, in that an adequately designed accounting system should incorporate methods and records that will satisfy the requirements of this

section.

(c) **Internal controls.**

(i) Upon the request of the department, the taxpayer must provide a description of the business process that created the retained records. Such description must include the relationship between the records and the tax documents prepared by the taxpayer and the measures employed to ensure the integrity of the records.

(ii) The taxpayer must be capable of demonstrating:

(A) The functions being performed as they relate to the flow of data through the system;

(B) The internal controls used to ensure accurate and reliable processing; and

(C) The internal controls used to prevent unauthorized addition, alteration, or deletion of retained records.

(iii) The following specific documentation is required for machine-sensible records retained pursuant to this section:

(A) Record formats or layouts;

(B) Field definitions (including the meaning of all codes used to represent information);

(C) File descriptions (e.g., data set name); and

(D) Detailed charts of accounts and account descriptions.

(7) **Access to machine-sensible records.**

(a) The manner in which the department is provided access to machine-sensible records may be satisfied through a variety of means that shall take into account a taxpayer's facts and circumstances through consultation with the taxpayer.

(b) Such access will be provided in one or more of the following manners:

(i) The taxpayer may arrange to provide the department with the hardware, software and personnel resources to access the machine-sensible records.

(ii) The taxpayer may arrange for a third party to provide the hardware, software and personnel resources necessary to access the machine-sensible records.

(iii) The taxpayer may convert the machine-sensible records to a standard record format specified by the department, including copies of files, on a magnetic medium that is agreed to by the department.

(iv) The taxpayer and the department may agree on other means of providing access to the machine-sensible records.

(8) **Storage-only imaging systems.**

(a) For purposes of storage and retention, taxpayers may convert hard-copy documents received or produced in the normal course of business and required to be retained under this section to microfilm, microfiche or other storage-only imaging systems and may discard the original hard-copy documents, provided the conditions of this section are met. Documents which may be stored on these media include, but are not limited

to, general books of account, journals, voucher registers, general and subsidiary ledgers, and supporting records of details, such as sales invoices, purchase invoices, exemption certificates, and credit memoranda.

(b) Microfilm, microfiche and other storage-only imaging systems must meet the following requirements:

(i) Documentation establishing the procedures for converting the hard-copy documents to microfilm, microfiche or other storage-only imaging system must be maintained and made available upon request. Such documentation must, at a minimum, contain a sufficient description to allow an original document to be followed through the conversion system as well as internal procedures established for inspection and quality assurance.

(ii) Procedures must be established for the effective identification, processing, storage, and preservation of the stored documents and for making them available for a period of five years.

(iii) Upon request by the department, a taxpayer must provide facilities and equipment for reading, locating, and reproducing any documents maintained on microfilm, microfiche or other storage-only imaging system.

(iv) When displayed on such equipment or reproduced on paper, the documents must exhibit a high degree of legibility and readability. For this purpose, legibility is defined as the quality of a letter or numeral that enables the observer to identify it positively and quickly to the exclusion of all other letters or numerals. Readability is defined as the quality of a group of letters or numerals being recognizable as words or complete numbers.

(v) All data stored on microfilm, microfiche or other storage-only imaging systems must be maintained and arranged in a manner that permits the location of any particular record.

(vi) There must be no substantial evidence that the microfilm, microfiche, or other storage-only imaging system lacks authenticity or integrity.

(9) Effect on hard-copy recordkeeping requirements.

(a) The provisions of this section do not relieve taxpayers of the responsibility to retain hard-copy records that are created or received in the ordinary course of business as required by existing law and regulations, except as otherwise provided in this section. Hard-copy records may be retained on a recordkeeping medium as provided in subsection (8) of this section.

(b) If hard-copy records are not produced or received in the ordinary course of transacting business (e.g., when the taxpayer uses electronic data interchange technology), such hard-copy records need not be created.

(c) Hard-copy records generated at the time of a transaction using a credit or debit card must be retained unless

all the details necessary to determine correct tax liability relating to the transaction are subsequently received and retained by the taxpayer in accordance with this section.

(d) Computer printouts that are created for validation, control, or other temporary purposes need not be retained.

(e) Nothing in this section prevents the department from requesting hard-copy printouts in lieu of retained machine-sensible records at the time of examination.

(10) **Out-of-state businesses.** An out-of-state business which does not keep the necessary records within this state may either produce within this state such records as are required for examination by the department or permit the examination of the records by the department or its authorized representatives at the place where the records are kept. RCW 82.32.070.