

# Japan's e-Storage Act: New Circular and Q&A explain changes under FY 2022 Tax Reform

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## In brief

As discussed in our previous Japan Tax Update, the latest round of Japanese tax proposals (the 'FY 2022 Tax Reform Proposal') contained various changes to Japan's e-storage rules, including a transitional measure that delays applicability of new mandatory provisions relating to e-storage of e-transaction data until January 1, 2024 (the 'Transitional Measure').<sup>1</sup>

On June 24, 2022, Japan's National Tax Agency ('NTA') released on its website an explanation of various e-storage provisions (the 'Circular'), and a Q&A (the 'Q&A') which was partially revised in light of the FY 2022 Tax Reform. The Circular and Q&A also respond to frequently asked questions by taxpayers regarding revisions to the e-Storage Act under the FY 2021 Tax Reform.

We discuss the main points from the Circular and the Q&A below.

## In detail

### 1. National Tax Books and National Tax-related Documents

#### (1) E-storage of national tax books as an image file or PDF

When e-storing national tax books, it is necessary, in principle, to be able to comply with the requirement for such data to be downloaded (that is, to respond to a request by an auditor to download and receive electronic records). When electronic records of national tax books are converted and stored in the form of an image file or PDF, however, the ability to search for specific content in such data is poor. The Q&A clarified that storing data in the form of an image file or PDF file does not comply with data storage requirements for national tax books, except under special circumstances, such as where data is stored in the form of CSV file as well, which allows for content searchability, etc.<sup>2</sup>

#### (2) Methods of saving copies of an invoice under e-storage rules

Where a taxpayer prepares an invoice using a personal computer, prints it out, affixes the representative seal, and sends the document to a counterparty, unless the taxpayer adds additional

<sup>1</sup> See previous Japan Tax Update at <https://www.pwc.com/jp/en/taxnews/pdf/jtu-20220124-en.pdf>

<sup>2</sup> Books and Documents Q&A, Question 22.

information in writing on the invoice prior to sending, the taxpayer may treat this as within the scope of national tax-related documents that the taxpayer has consistently prepared using a computer.<sup>3</sup>

Also, when e-storing national tax-related documents, it is necessary in principle to store the electronic data in the same condition as when it was sent to the counterparty. When the database that a taxpayer uses automatically converts the underlying data into a standard invoice format, however, e-storage requirements can be met if satisfied with regard to the data in the database, rather than to the actual copies of invoices. In the taxpayer is relying on data in its database, it is also necessary for the taxpayer to be able to provide the invoice in the same condition as when sent to the counterparty, if requested by a tax official during a tax examination.<sup>4</sup>

## **2. E-Storage of Scanned National Tax-related Documents**

### **(1) Meaning of 'ordinary length of time to process materials'**

The e-Storage Act regulations stipulate that the deadline to input data via scanner storage is promptly after the 'ordinary length of time to process materials'. The meaning of this deadline was previously explained as shortly after 'the length of the business cycle required to process national tax-related documents, from the time such materials are prepared or received until the documents can be read by the scanner'.<sup>5</sup> As a result of the revisions to the Circular, the meaning is now understood as shortly after 'the ordinary length of the business cycle, from the time that the taxpayer prepares or receives national tax-related documents, to the time that the taxpayer inputs the data or affixes the timestamp'.<sup>6</sup>

### **(2) Accreditation of timestamps**

It was previously stipulated that only timestamps approved by the Japan Data Communications Association ( 'DEKYO') could be used for e-storage purposes under the e-Storage Act. With the establishment of the time stamp accreditation system by the national government, however, timestamps authorized by the Minister of Internal Affairs and Communications should be affixed to digitally stored national tax-related data or e-Transaction data from April 1, 2022 onwards. Note that a transitional measure applies for the period from April 1, 2022 until July 29, 2023, such that it should be acceptable for taxpayers to use timestamps made by companies that received approval by DEKYO. Details of time certification via timestamps authorized by the Minister of Internal Affairs and Communications are addressed in the Circular and Q&A.<sup>7</sup>

## **3. E-Transaction Data**

### **(1) Scope of e-transactions in the case of different forms of payment**

When a taxpayer makes a direct electronic tax payment to the tax office via the e-Tax System, a notice of receipt (notification of payment classification number and notification of completion of payment) is stored in the taxpayer's mailbox. In making an e-tax payment, the taxpayer would remit the tax directly to the Bank of Japan, so the Tax Office would not be required to issue information equivalent to a 'receipt' to the taxpayer. Therefore, the notice of receipt would not fall within the scope of e-transaction data that would need to be stored by the taxpayer. The taxpayer must however maintain receipts issued when the taxpayer pays cash to the tax office at the tax office

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<sup>3</sup> According to Arts 4-1 and 4-2 of the e-Storage Act, National Tax-related documents that are not consistently prepared using a computer may not be stored digitally as scanned documents.

<sup>4</sup> Books and Documents Q&A, Question 25.

<sup>5</sup> See e-Storage Act, Circular 4-18.

<sup>6</sup> Circular 4-18.

<sup>7</sup> Circular 4-22, etc.

counter or statements that contain transaction information related to receipts when the paying through an ATM.<sup>8</sup>

In addition, remittances using internet banking would in principle be considered EDI transactions and thus within the scope of e-transactions. In this case, it is necessary to download the electronic record of the document (including the remittance date, amount, counterparty name, etc.) which would be on a document issued by a financial institution if payment were made over the counter, or to save the data as a PDF file.<sup>9</sup>

(2) E-transaction data that has been edited in a reasonable manner

A. Saving Encrypted Data

Under E-Storage Act rules that address maintaining e-Transaction data digitally, e-transaction data should not be stored in its encrypted form, but rather the data received should be stored after conversion by a translator. Likewise, information sent by a taxpayer should be stored before conversion by translator. Because from a data security standpoint it is common to store data in its encrypted form, however, if the encrypted data can be swiftly reverted to an unencrypted file during a tax investigation, the authorities should also permit the storing of encrypted files.<sup>10</sup>

B. Conversion to a company's code

The Circular addresses the issue of codes included in EDI data that a taxpayer receives from a transaction counterparty. When a taxpayer uses a pre-defined conversion protocol to convert codes in EDI data into the taxpayer's own company codes without changing the content of the data, the Circular clarified that this should also be considered 'editing in a reasonable manner'. The Circular notes, however, that even in such a case, manual data entry may result in unintentional errors, so the code conversion must be performed automatically, and the conversion protocol must also be saved, so that the taxpayer is able to clearly explain the content of the underlying transaction represented by the information code to an auditor.<sup>11</sup>

C. Converting to a PDF file or removing a password

When a taxpayer receives a file in Excel or Word file format and converts and saves it as a PDF file, or removes a password from a password protected file, such edits can be undertaken without changing the underlying transaction data. The Q&A clarified that such edits would be classified as 'editing in a reasonable manner'.<sup>12</sup>

D. How to store data from invoices issued by taxpayer

The Q&A clarified rules relating to data for invoices or the like issued by the taxpayer. If the data content is automatically output from the taxpayer's invoice database, which is the source of the transmitted data, and there is no risk that the content of the data would be changed after the transaction, such that the data can be considered to have satisfied the conditions of being edited in a reasonable manner, the Q&A makes clear that storing data in the taxpayer's database should be regarded as satisfying relevant requirements. (That is, the taxpayer does not need to save the underlying invoices issued to the counterparty.) In such a case, it is necessary, however, for the

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<sup>8</sup> e-Transaction Q&A, Question 8.

<sup>9</sup> e-Transaction Q&A, Question 9.

<sup>10</sup> Circular 7-1.

<sup>11</sup> e-Transaction Q&A, Question 36.

<sup>12</sup> e-Transaction Q&A, Question 37.

taxpayer to be able to output the information in the format that was actually provided to the transaction counterparty upon request by an auditor in a tax examination.<sup>13</sup>

(3) Transaction timing in e-transaction involving the download of data from a website

The Q&A provided additional rules regarding receipts and other data that can be downloaded from a website. The Q&A notes that the taxpayer should in principle save such materials at the time such electronic records of e-transactions can be confirmed on an internet website, and the taxpayer should be considered to receive the digital data relating to the e-transaction at that time. If, however, the taxpayer is not notified by e-mail or other means that the data has been released on a website, it should be acceptable for the taxpayer to store the relevant data at 'an appropriate time'.<sup>14</sup> Note that if a (physical) document with the same transaction data as that appearing on the website is sent to the taxpayer by mail, the taxpayer is only required to maintain the original version of the material (whether it is the digital version or the hard copy).<sup>15</sup>

(4) How to satisfy the search function requirements when a taxpayer receives a PDF containing multiple invoices

In order to satisfy the search function requirements for e-transactions under the e-Storage Act, the search results must display specific records in an orderly and clear format. If a taxpayer receives a PDF file containing multiple invoices, separating the PDF into individual PDF files for each transaction, for example, made without editing the underlying transaction data, should be considered 'editing in a reasonable manner'. The taxpayer should name and manage the separated PDF files appropriately and the taxpayer should be able to comply with a request from tax officials to download the files. If the taxpayer separates the PDF into multiple PDFs in this manner, the separated PDF files should also be treated as satisfying the search requirements.<sup>16</sup>

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### The takeaway

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Japan's e-storage rules were significantly revised in FY 2021, allowing taxpayers to save documents digitally more easily in practice. Taxpayers had expressed concern, however, that certain issues in connection with the new rules remained somewhat unclear in practice. The Circular and Q&A address a number of such points.

Clarification to existing rules is important, especially as taxpayers prepare to comply with provisions regarding e-transaction data that will become mandatory from January 1, 2024. With this deadline rapidly approaching, this is the time to ensure that your company's document retention status is compliant with existing requirements, and with new requirements slated to come into effect in 2024.

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<sup>13</sup> e-Transaction Q&A, Question 40.

<sup>14</sup> Although the wording of the revised Q&A remains vague, it would appear that the taxpayer would not be strictly required to download the data at the time the data is released on the internet.

<sup>15</sup> e-Transaction Q&A, Question 39.

<sup>16</sup> e-Transaction Q&A, Question 46.

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**Let's talk**

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We would be happy to discuss how these rules may apply to your company, or to answer any questions. Please feel free to contact us.

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