



**iPayables Compliance with IRS Regulations on
Electronic Transactions**

iPayables Position Paper
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What are the current IRS rules regarding transmission and storage of electronic transactions?

The pertinent governing regulations are:

- Internal Revenue Code Section 6001
- Revenue Procedure 91-59
- [Revenue Procedure 97-22](#)
- [Revenue Procedure 98-25](#)

1) Internal Revenue Code Section 6001 – Requirements for book & record retention (hardcopy).

2) Revenue Procedure 91-59 - IRS Code states, "any person subject to income tax...must keep such books and records...required to be shown by that person in any return of such tax or information." Revenue Procedure 91-59 says that this applies to:

- All paper records
- Electronic records for tax years commencing prior to 1/1/98.

3) Revenue Procedure 97-22

"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."

In essence the institutions computer system must:

- Be accurate and reliable;
- Insure integrity and provide reasonable controls to prevent alterations;
- Be inspected periodically;
- Reproduce a legible hardcopy or computer monitor view that is at least as legible as the original paper version;
- Be indexed;
- Have an audit trail from original entry to the tax return;
- At the time of an exam, audit, evaluation, etc. by the IRS, resources must be provided to the IRS for retrieval of information;
- Also note that these rules apply to those institutions or firms who have subcontracted their records management to a third party.

4) Revenue Procedure 98-25

The purpose of this revenue procedure is to specify the basic requirements that the Internal Revenue Service considers to be essential in cases where a taxpayer's records are maintained within an Automatic Data Processing system (ADP) which uses or incorporates EDI technology or an electronic storage system.

This procedure makes document retention requirements uniform and sensible. It applies to:

- All taxpayers with assets of \$10 million or higher;
- Some smaller taxpayers;
- All controlled foreign corporations;
- All insurance companies.

This practice applies if:

- Records are only in machine sensible form (i.e. EDI based transactions);
- Machine sensible records are used for computations, it can not be easily recomputed without a computer;
- You use a third party to provide services.

States that:

- Computerized records are books and records as defined by the IRS;
- Computerized records are books and records as defined by the IRS;
- Records must be retained to provide a proper audit trail from original entry to the tax return;
- A computer record is sufficient evidence and does not require a duplicate paper record copy.

Machine sensible records (i.e. EDI based transactions) must:

- Be retained as long as they are required Provide sufficient information to support and verify tax return and reconcile with tax payers books;
- Be made available to the IRS and be capable of being processed;
- Is retained after disposition of a subsidiary.

Must maintain and make available documentation of the business processes that:

- Create the retained records;
- Modify and maintain its records
- Evidence the authenticity and integrity;
- Must establish and document audit trails spelled out in this revenue procedure.

The taxpayer must:

- Provide the IRS with resources necessary to process taxpayers machine sensible books and records;
- Notify the IRS if any machine sensible records are lost, stolen, destroyed or otherwise no longer capable of being processed.

Specific EDI Technology is addressed in Revenue Procedure 98-25. The following are excerpts from this Revenue Procedure:

Use of EDI Technology (Section 5.03):

Machine-sensible records alone, or in combination with any other records (e.g., underlying contracts, price lists, and price changes), must contain all the information of hardcopy books and records.

For example, a taxpayer that uses EDI 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 retain the incoming EDI transactions. Neither the EDI transactions, nor the accounts payable system, contain product descriptions or vendor names. To satisfy the requirements, the taxpayer must supplement its EDI records with product code description lists and a vendor master file.

A taxpayer may capture the required detail for an EDI transaction at any level within its accounting system. However, the taxpayer must establish audit trails between the retained records and the taxpayer's books, and between the retained records and the tax return.

Section 11.02 of this revenue procedure provides additional guidance concerning hardcopy requirements related to EDI transactions.

HARDCOPY RECORDS (Section 11.02)

A taxpayer need not create or retain hardcopy records if:

- The hardcopy records are merely computer printouts created only for validation, control, or other temporary purposes;
- The hardcopy records are not produced in the ordinary course of transacting business (as may be the case when utilizing EDI technology); or
- All the details relating to the transaction are subsequently received by the taxpayer in an EDI transaction and are retained as machine-sensible records by the taxpayer in conformity with this revenue procedure. For example, a taxpayer need not retain credit card receipts generated at the time of a transaction if all pertinent information on the receipts is subsequently received in an EDI transaction and retained as a machine-sensible record. See section 5.03 of this revenue procedure for requirements relating to EDI.

DEFINITIONS

"ADP System" - consists of an accounting and/or financial system (and subsystems) that processes all or part of a taxpayer's transactions, records, or data by other than manual methods. An ADP system includes, but is not limited to, a mainframe computer system, stand-alone or networked microcomputer system, Data Base Management System (DBMS), and a system that uses or incorporates Electronic Data Interchange (EDI) technology or an electronic storage system.

"EDI technology" - is the computer-to-computer exchange of business information.

"Electronic Storage System" - is a system used 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. See Rev. Proc. 97-22, 1997-13 I.R.B. 9, for electronic storage system requirements.

"Machine-sensible Record" - is data in an electronic format that is intended for use by a computer. Machine-sensible records do not include paper records or paper records that have been converted to an electronic storage medium such as microfilm, microfiche, optical disk, or laser disk.

NOTE: Please consult Tax Advisor for specifics and additional guidance.

iPayables Compliance with IRS Electronic Transaction Standards

iPayables (the service) complies with or exceeds the IRS Standard that electronic transactions be kept in a manner "equivalent to paper" in the following ways.

- The transmission of the data is secured using SSL (Secure Socket Layer) technology from the point of origin (the vendor) to iPayables.
- The vendor is required to supply id/password combinations to access the service, ensuring the identity of the vendor.
- Once the data is in iPayables, all access to the data is controlled by the iPayables web interface which, once again, is secured using SSL.
- The data is stored by iPayables in two fashions.
 - First the data is stored in a Relational Databases (RDBMS), indexed, for rapid access.
 - The data is also extracted weekly to an XML Archive that is stored on CD. XML is used to ensure that the archive data is human readable as well as machine searchable.
- Database access is restricted to authorized users via username, password with restriction on rights within the databases.
- All changes to invoice data that occurs after the vendor has submitted the invoice, per vendor and/or customer, are logged with attending audit information regarding who changed the information.
- At any time an invoice can be "devolved" to the original state.
- All invoices are tracked internally at iPayables using a unique "document number".
- When invoices are transmitted to a customer, the encryption/authentication method is determined by the customer, but iPayables recommends either using VPN tunnels (the data stream is encrypted) or PGP Encryption (the file is encrypted prior to transmission). Each of these methods ensure that the data is not modified in transit.
- To properly tie invoices in the customer A/P system to iPayables invoices the customer would need to store iPayables Invoice Document Number in their (the customers) A/P System.
- When this is not possible invoices are matched using Vendor ID, Invoice Number, and Invoice Date.
- All processes involved in the creation, modification, retention of invoices is documented.

- Audit trail processes are documented.
- All retained data is stored off site in read-only, encrypted format.

“A taxpayer may capture the required detail for an EDI transaction at any level within its accounting system. However, the taxpayer must establish audit trails between the retained records and the taxpayer’s books, and between the retained records and the tax return.”

In this way the customer (taxpayer) has the option of retaining the invoice data from completed and verified EDI transactions in its accounts payable system or retain the incoming EDI transactions.

Summary

iPayables provides the same level of reliability and security as paper because it gives you the same evidence of each transaction – all information contained in a paper based invoice is contained within an electronic invoice. With iPayables, not only are organizations freed from the expense of manually processing paper based invoices, but the security and audit trail of each record is actually increased. iPayables not only meets but exceeds the IRS regulations providing an additional level of assurance.