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**Forum on Strategic Management  
Sub-group on Electronic Commerce**

**PDA STANDARD TAX AUDIT FILE**

**(Note by the Delegate from the Netherlands)**

*This document is submitted to the FSM Sub Group on Electronic Commerce FOR INFORMATION at its meeting to be held on 29-30 November 1999 at the Château de la Muette.*

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## PDA STANDARD TAX AUDIT FILE

(Note by the Delegate from the Netherlands)

### Introduction

1. In the Netherlands it was recently decided to introduce a standard audit file. The standard audit file is a digital file in a fixed record format that contains predefined data elements. The tax administration has built a custom made software program (CLAIR) that makes use of this standard audit file in the event of a tax audit. CLAIR has a number of built-in standard queries that can be of use during a tax audit. The tax auditor can also define his own queries. The objective of the standard audit file/ CLAIR concept is twofold:

- It has to provide businesses (especially SME's) with a simple method to meet their retention requirements (for digital accounting data) for tax purposes and
- It has to provide the tax auditor with a standard tool that gives easy access to this retained accounting data in the event of an audit.

2. This paper explains the background for defining the concept.

### Administration requirement

3. Within The Netherlands subjects to Income taxes (who carry on a business), V.A.T. or Wages taxes are required to keep an administration. The administration consists of, inter alia, the accounting data in the ledgers and the source documents. The retention period is in general 7 years. The accounting data in the ledgers is almost always kept in an electronic form, also in the case of small businesses. Except for E.D.I., most external source documents are kept in paper form. In the event of an audit, the tax auditor wants to have a copy of the accounting data in the ledgers in electronic form in stead of in paper form. Using Computer Assisted Audit Techniques (C.A.A.T.'s) the audit can be performed in a more efficient and effective way which is in the interest of both the tax administration and the audited organisation because the time to perform the audit can be limited .

4. When the use of electronic copies by tax auditors was introduced in the 1980's most organisations only held copies of the accounting data of the current year and didn't retain copies of older years. The data of older years was printed on paper. Some tax advisors disputed the right of the tax administration to have copies in electronic form. The General Tax Act of that time stated that, if required, *books and other documents* must be provided for inspection when cognisance could be of interest for determining the facts that could influence taxation. The tax advisors were of the opinion that electronic copies of a administration could not be regarded as books or other documents. In 1989 a draft act was send to parliament to change the relevant wording. After extensive consultation with the business community the revised wording passed in 1994.

5. The goal of the new wording was to define an administration requirement in a technology independent way because the storage media for digital data developed in a rapid pace. When asked,

everyone is required to provide the tax inspector with books, documents and other *data carriers* of which reference could be of interest for determining the facts that could influence taxation. It is the choice of the tax inspector to ask for the original data or the contents of it (electronic copy). The administration must be kept in a form that enables the tax auditor to perform the audit within a reasonable term. Everyone who is required to keep an administration may convert data from one carrier to another, provided that this conversion is done correct and complete and the data is retained for the retention period. The data must be made readable within a reasonable term. As a general rule, conversion from an electronic carrier to paper is not allowed, because this has a negative effect on the accessibility and therewith the efficiency of an audit. An exception is made for very small companies. The use of C.A.A.T.'s within such a small company has only a limited benefit compared to paper records of account.

### **Experiences with the 1994 administration requirement**

6. During the period 1994 to 1995 the tax auditors were faced with the fact that a lot of organisations were not aware of their requirement to keep accounting data in an electronic form. This was especially the case in SME's. Another experience was that SME's often worked with packaged software and didn't have the tools, knowledge and hardware capacity to retain the accounting data in a proper way. These experiences were the trigger for retention reviews. The goal of these retention reviews was to ensure that all the necessary data was retained and available in an accessible format. The retention reviews in smaller companies showed that the retention requirements for these organisations, with packaged software, were often very burdensome. The problem was that the time between the versions of the packaged software was very short. The new packages were often not able to use the data from older years because the record lay-out was changed and only the current figures were migrated. This led to the advice of the tax administration to store the records in a platform independent way; e.g. flat ASCII. Most software packages, and also the C.A.A.T.'s that are being used by the tax administration, can import those data. In most cases, the software packages are not able to export all the entered data in ASCII format. This was the start of the definition of a standard audit file.

### **Idea behind the audit file**

7. Starting from the advice of the tax auditors to store accounting data in a flat ASCII format it was recognised that standardisation of such a flat file could have benefits for business as well as the tax administration.

8. If the tax administration would define a standard format this would mean that suppliers of standard software could implement an export option into their software that creates a file in this standard format. As long as the packages have this built-in export function they can change the internal record lay outs of the package as much as they like in new versions without consequences. The SME's that make use of those packages would not have to bother any more about the way the accounting data is technically stored. They just produce the audit file, knowing that this meets the retention demands of the tax administration. Another benefit for the business is the efficiency of a tax audit (reduction of time to perform a tax audit).

9. There is also a clear benefit for the auditors of the tax administration. They can copy the retained audit files and use them in their own audit software. If the format of the audit file is the same in every business it would even be possible to build a custom-made tax audit program with predefined query possibilities. This tax audit program can be used by every tax auditor, regardless the extend of his knowledge of (recent) IT. The use of this software means that an audit can be performed in a more efficient way. This not only benefits the tax administration but the audited entity as well.

10. The intention is to implement the concept at the end of 1999.

#### **Data elements of the audit file**

11. The use of the standard audit file has no impact on the administration requirement and is optional. All the source documents and accounting data have to be retained for the retention period. The audit file is just a standardisation of the way in which accounting data is stored. If a business makes use of data elements that are not defined in the standard audit file they have to retain these elements too. Practice shows that different entities use different data elements in their ledgers depending on the business therein. If the audit file is to be successful it has to be applicable in most businesses. This means that the data elements that are used in different branches have to find their place in the audit file. On the other hand, the question arose if it was efficient to define all data elements, even those elements that were only used in a very specific branch with little volume.

12. An inventory was made of frequently used standard accounting packages in the business community. The record lay-out of these packages were analysed and the result was an inventory of the data elements that were used and stored in these packages. A selection was made of the necessary data elements and the format of these data elements was defined. This resulted in the record lay-out of the audit file. The record lay-out is defined in annex I. The data elements are shown in annex II.

13. From the viewpoint of security the tax administration in The Netherlands works with a nearly completely closed technical environment. All the data on a disk of a computer of a tax auditor is encrypted. In order to exchange the data from the taxpayer to the tax administration a compression and security application has been developed. The compression technique is a public domain compression algorithm. The application makes use of a key that is developed by the tax administration to secure the data. This exchange application is made available free of charge.

#### **Standpoint business community/ tax advisors / software suppliers**

14. The initiative has been discussed with the representatives of the business community, the tax advisors and software suppliers. They all recognised the possibilities of the audit file and were willing to accept the concept. The business community welcomes the fact that the use would mean less time to comply with tax regulations and a more efficient tax audit. It was calculated that the broad implementation of the standard audit file could lead to a yearly savings of  $\pm 9$  million EURO for the business community. Although a tax audit can be performed in a more efficient way, the business community also pointed out that this must not lead to unnecessary audits. The software suppliers stated that the costs to build in the export facility would be limited. In most cases, this export facility could easily be built in. All parties stated that the audit file can only be a success if the confidentiality of the accounting data is ensured by the tax administration.

15. The four largest players in financial software for SME's in the Netherlands, with a market share of 80%, already have supported the concept and adapted their software to produce the standard audit file. It is expected that most of the other players will adapt the concept in the near future.

**Standard tax audit software (CLAIR)**

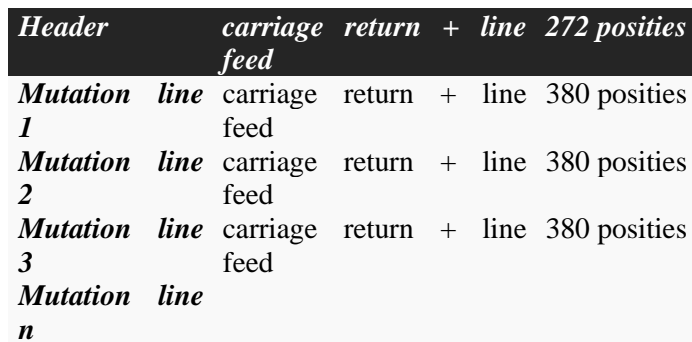
16. The tax administration in The Netherlands has developed its own standard tax audit software: CLAIR. The acronym stands for Clear Look At Information Retrieved. It makes use of a copy of the audit file that is produced within an entity. Conversion is not needed anymore, the record lay-out is pre-defined in CLAIR. CLAIR has a number of frequently used predefined queries. The tax auditor also has the possibility to define his own, case dependant, queries.

**Future developments**

17. If the concept of the standard audit file /CLAIR proves to be a success there are other possibilities for expanding the concept to other areas of the administration of the business, e.g. the wages records. The benefits for both the business as well as the tax administration would increase with such an expansion.

ANNEX I

The audit file starts with a header (first line). The next are mutation lines. This can be represented in the next diagram.



The contents of the header is as follows:

Name data element	Compulsory/ optional	Format	Length	Allign	Special requirements
<b>Version audit file</b>	comp	CHAR	12		Content: CLAIR1.00.00
<b>Bookkeeping package + version</b>	opt	CHAR	50		
<b>Administration code</b>	opt	CHAR	20	left	
<b>Year/period</b>	comp	CHAR	15	left	
<b>Fiscal number</b>	opt	CHAR	15	left	
<b>Name</b>	comp	CHAR	50	left	
<b>Address</b>	opt		30		
<b>City</b>	opt		30		
<b>Number of mutations</b>	opt	N	10		
<b>Date making</b>	opt	D	8		
<b>Sum debit entries</b>	opt	CHAR	16		
<b>Sum credit entries</b>	opt	CHAR	16		

Example:

0	1	2	3	4	5	6	7	8	9	10	11	12	13	14		
0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789		
CLAIR1.00.00						Package X version 2..5			25		1998		094643441		Bike shop de Waard	
15	16	17	18	19	20	21	22	23	24	25	26	27				
0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	012				
Herculesplein 235				Amsterdam			248		29041999		1847485		1847485			

ANNEX II

A mutation line looks like this:

Data element	Compulsory/ optional	Format	Length	Align
Journal	opt.	CHAR	20	left
Journal description		CHAR	30	left
Period	opt.	NUM	4	right
Reference number	opt.	NUM	10	right
Line number	opt.	NUM	3	right
Processing date	opt.	DATE	8	left
Account number	comp	CHAR	15	left
Sort Account number	opt.	CHAR	5	left
Cluster Account number	opt.	CHAR	15	left
Account name	comp	CHAR	30	left
Mutation date	comp	DATE	8	left
Voucher number	opt.	CHAR	15	left
Sort Mutation	opt.	CHAR	5	left
Relation other administration	opt.	CHAR	15	left
Description	comp	CHAR	30	left
Debit amount	comp	NUM	16,2	right
Credit amount	comp	NUM	16,2	right
VAT code	opt.	CHAR	3	left
Currency	opt.	CHAR	3	left
Currency rate	opt.	NUM	13,6	right
A/P or A/R Number	opt.	CHAR	15	left
A/P or A/R sort	opt.	CHAR	5	left
A/P or A/R name		CHAR	30	left
A/P or A/R address		CHAR	30	left
A/P or A/R ZIP code		CHAR	8	left
A/P or A/R City		CHAR	30	left

Examples:

0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	
0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	
30		Memo			0		01011998	000000000000100	B	100		Building		15051998	00
20		Bank			5		23051998	000000000001200	B	200		Accounts receivable		28061998	00
10		Cash			7		11071998	000000000004250	VB	400		Petrol costs		12071998	00
15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	
0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	
000098000001				Balance at 01.01			1854500,00			HFL	1,00				
000098000123				Invoice 9804123				21438,57		HFL	1,00	120034	D	V.O.F. Bruggeman	
00009801268K				Gasstation Central			112,70		2	HFL	1,00				
30	31	32	33	34	35	36	37	38							
0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0123456789	0							
		Korte Dwarskade 256			4829 PP	Hazerswoude									