



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

COMMISSIONER

March 5, 2007

MEMORANDUM FOR RICHARD J. MORGANTE
COMMISSIONER, WAGE AND INVESTMENT DIVISION

FROM: Mark W. Everson 
Commissioner of Internal Revenue

SUBJECT: Guidance for the Use of Binding Arbitration Under
the Administrative Dispute Resolution Act Of 1996

I am committed to the early and expeditious resolution of challenges to decisions that affect the Free File Alliance, LLC (Alliance) members or new market entrants' ability to post a listing on irs.gov. After consultation with the Department of Justice, I have decided to implement the use of binding arbitration to resolve certain disputes that may arise between the IRS, or the IRS and the Alliance, and Alliance members or new market entrants.

In accordance with the attached guidance, binding arbitration before the Civilian Board of Contract Appeals, as successor to the General Services Board of Contract Appeals, will be used to resolve disputes under Article VIII of the Memorandum of Understanding on Service Standards and Disputes between the IRS and the Alliance. Binding arbitration may be invoked by an Alliance member or new market entrant to challenge the rejection of an Alliance member or new market entrant's offering, the removal of an Alliance member's listing on irs.gov, or rejection of an Alliance member's request that its listing be restored by the IRS, or the IRS and the Alliance.

The use of binding arbitration is entirely voluntary and was implemented at the request, and with the concurrence, of the Alliance. This guidance will provide us with a tool to help achieve our goal of providing expedited, effective, efficient and fair resolution of Free File program related controversies.

Attachment

Guidance for the Use of Binding Arbitration Under the Administrative Dispute Resolution Act Of 1996

Background

In 2001, the President's Management Council announced, through the Office of Management and Budget (OMB), the establishment of 24 initiatives that will expand e-services within the federal government, including the Free File Initiative (formerly known as EZ Tax Filing). The objective of the Free File Initiative is to decrease the tax preparation and filing burden of wage earners by providing greater access to free online tax preparation and filing options for a significant number of taxpayers. This has been accomplished by the formation of a partnership between the Internal Revenue Service (IRS) and the Free File Alliance, LLC (Alliance) a consortium of tax industry companies. The Alliance provides an online marketplace through which participating companies offer their free tax preparation and filing services to certain segments of the taxpayer population.

Each year the IRS receives well over 200 million tax returns and 1.4 billion information returns (e.g., W-2s, 1098s, 1099s), issues 106 million individual refunds, handles over 77 million taxpayer assistance calls, and collects more than \$2.0 trillion.¹ While many of these transactions are processed electronically, many are not.² In 2005, for the first time, the volume of individual income tax returns filed electronically exceeded the volume of tax returns submitted on paper.³ Within this context, the IRS Restructuring and Reform Act of 1998 (RRA 98) was enacted in part to introduce new procedures that would leverage electronic government capabilities to reduce overall taxpayer burden and improve processing efficiencies. RRA 98 established a goal that 80 percent of all tax and information returns should be filed electronically by 2007. In response, the IRS Electronic Tax Administration (ETA) established nine key strategies to expand its existing user base of electronic filing services.⁴ The partnership between the IRS and the Alliance directly supports three of those strategies:

1. Make electronic filing, payment and communication so simple, inexpensive and trusted that taxpayers will prefer these to calling and mailing;
2. Substantially increase taxpayer access to electronic filing, payment, and communication products and services; and
3. Encourage private sector innovation and competition.

The Free File Initiative was implemented by a three year agreement (Free File Agreement) between the IRS and the Alliance, which was published in the Federal Register (Vol. 67, No. 153, page 51621) on August 8, 2002, and executed on October

¹ IRS Data Book: 2004, <http://www.irs.gov/pub/irs-soi/04databk.pdf>

² IRS e-Strategy for Growth, *Electronic Tax Administration*, Internal Revenue Service, Department of the Treasury, Publication 3187 (Rev. 1-2005)

³ 2005 Filing Season Statistics (10/21/2005), <http://www.irs.gov/taxstats/article/0..id=96629.00.html>

⁴ IRS e-Strategy for Growth, *Publication 3187* (Rev. 1-2005)

30,2002. On October 29,2005, the Free File Agreement was amended and extended for an additional four years. IRS Free File first launched on January 16, 2003, with 17 Alliance companies offering free online tax preparation and e-filing services. Since the initial debut, more than 15 million tax returns have been e-filed using IRS Free File services. In 2006, approximately 4 million tax returns were e-filed through Free File with 20 Alliance companies participating in the initiative.

Initiative Description

To accomplish the strategic objectives outlined above, the IRS and the Alliance work together to offer free, online tax return preparation and filing services to taxpayers. The Alliance offers tax preparation and filing services to taxpayers at no cost; the IRS provides taxpayers with links to the free services through a web page hosted on irs.gov, with links from other appropriate government sites. Under the current Free File Agreement:

- ▶ The Alliance, as a whole, will offer free online tax preparation and electronic filing to 70% of all individual taxpayers.
- ▶ Alliance members will meet online tax preparation and filing field and corporate stability experience and expertise standards established by the IRS and the Alliance.
- ▶ Alliance members will comply with applicable security and privacy of taxpayer data regulations. Each member must have a third-party security and privacy certification that demonstrates best practice standards. Additionally, the Alliance, or its individual members, will annually (after April 25, 2006) conduct penetration and vulnerability assessment of individual member companies prior to the start of the filing season.
- ▶ Alliance members will meet a graduating performance standard for acceptance of electronic returns. For 2006, the minimum acceptance rate will be placed at 60 percent of electronic returns. The minimum acceptance rate will be gradually increased in future years based on discussions with the Alliance. Any member failing to meet the minimum acceptance rate may be removed from irs.gov.
- ▶ The IRS Free File Website will be developed as part of irs.gov, and will be hosted on IRS infrastructure. Other appropriate government web sites, such as FirstGov.gov, may link to the Free File page.
- ▶ Alliance members will create and supply proposed content for the IRS Free File Website but development and content management will be the responsibility of the IRS.
- ▶ The IRS Free File Website will list the free offerings in a manner consistent with the tier membership system described in the Alliance's Amended and Restated Operating Agreement (Operating Agreement). Each offering will clearly and plainly state the eligibility requirements for free use of a particular product/service.

- ▶ The IRS and the Alliance will provide a dispute resolution process that may be invoked by Alliance members whose offerings are rejected or removed from irs.gov.

Importance of the Use of Binding Arbitration

Among the benefits of using binding arbitration to resolve certain disputes between the IRS and Alliance members are time savings, cost savings, improved program management and increased satisfaction. Adoption of this dispute resolution process will help ensure the stability and sustainability of the Free File Initiative.

Time Savings

A major challenge the IRS and the Alliance face in dispute resolution is the need to quickly resolve disputes or controversies that may arise just prior to, or during, the peak filing period (January through April). For each filing season, the IRS receives approximately 95% of all federal individual income tax returns during this period. Similarly, 97% of all Free File returns are electronically submitted to the IRS during this four month period. Any delay in resolving disputes or controversies may prove to be detrimental not only to an individual Alliance member's ability to participate in the Free File Initiative during peak filing season, but may adversely affect the overall program by delaying the delivery of Free File services to taxpayers and/or limiting consumers' choices of available Free File products and services.

Cost Savings

Binding arbitration is a more cost efficient method of resolving covered disputes and /or controversies. The time savings described above directly correlates with cost savings. Additionally, as monetary relief is precluded under these guidelines and the Free File Agreement, the possibility of a costly adverse decision, as well as the expense of lengthy litigation, is eliminated.

Improved Program Management

The IRS and the Alliance agreed that in order for the Free File Initiative to operate efficiently, the authority of the IRS to render decisions, unilaterally or in concert with the Executive Director of the Alliance, concerning Alliance members' compliance with Free File Initiative requirements required clarification. Additionally, with this clarification, the Free File Agreement needed to include a dispute resolution process that would allow members to formally address the IRS' individual, or joint decision with the Alliance, to refuse to permit a member to list its company on the IRS website and/or the IRS' individual, or joint decision with the Alliance, to remove a company's listing from the IRS website. The Free File Agreement, as amended, along with a Memorandum of Understanding on Service Standards and Disputes (MOU) entered into on January 24, 2006, between the IRS and the Alliance allows the parties to manage the program in a manner which permit the IRS and the Alliance to solely or jointly take action against

Alliance members who are not in compliance with the terms of the Free File Agreement or MOU. Binding arbitration will provide Alliance members with a process to challenge the IRS' individual, or joint decision with the Alliance, to refuse to permit a member to list its company on the IRS website and/or the IRS' individual, or joint decision with the Alliance, to remove a company's listing from the IRS website.

Scope of the Use of Binding Arbitration

Alliance member may invoke binding arbitration to resolve a dispute involving the IRS' individual decision, or joint decision with the Alliance, to refuse a member's listing on the IRS website. Binding arbitration may also be invoked to resolve a dispute involving the IRS' individual decision, or joint decision with the Alliance, to remove a company's listing from the IRS website under the terms of the Free File Agreement and/or the MOU.

Overview

The following guidance is aimed at satisfying the requirements regarding binding arbitration specified within the Administrative Dispute Resolution Act (ADRA) of 1996.

Statutory Requirements

A. Considerations for Not Using Arbitration

The ADRA of 1996 calls for agencies to consider not using any form of ADR, including binding arbitration, in a number of specified circumstances. See 5 U.S.C. § 572(b). Binding arbitration between the IRS, the Alliance, and Alliance members, in accord with subsection 8.2 of the MOU, would not implicate any of these circumstances.

B. Other Statutory Requirements

In accordance with the ADRA of 1996, the following shall apply to all arbitrations conducted for covered Free File Initiative disputes.

1. The decision to arbitrate must be voluntary on the part of all parties to the arbitration. (See 5 U.S.C. §575(a)(1)).
2. A party may limit the issues it agrees to submit to arbitration. (See 5 U.S.C. §575(a)(1)(A)).
3. A party may agree to arbitrate on the condition that the award is limited to a range of possible outcomes. (See 5 U.S.C. §575(a)(1)(B)). Note: Pursuant to this guidance, all awards will be non-monetary. The range of possible outcomes is limited to rejecting the member or new market entrant's challenge or directing the IRS, or the IRS and the Alliance, to list or relist the member or new market

entrant on the IRS Free File Website. No other relief, including attorney fees, or other monetary awards of any kind, may be offered.

4. An agreement to arbitrate must be in writing. It must set forth the subject matter submitted to the arbitrator, and must specify the maximum award or "cap" that may be granted by the arbitrator. (See 5 U.S.C. §575(a)(2)). (Note: Pursuant to this guidance, all awards will be non-monetary. The range of possible outcomes is limited to rejecting the member or new market entrant's challenge or directing the IRS, or the IRS and the Alliance, to list or **relist** the member or new market entrant on the IRS Free File Website. No other relief, including attorney fees, or other monetary awards of any kind, may be offered).

The IRS shall not require anyone to consent to arbitration as a condition of entering into an agreement or obtaining a benefit. (See 5 U.S.C. §575(a)(3)).

An officer or employee of the IRS who offers to use arbitration must otherwise have the authority to enter into a settlement concerning the matter or must be specifically authorized to consent to the use of arbitration. (See 5 U.S.C. §§575(b)(1) and (2)).

7. The IRS and the Alliance have agreed that the arbitration will be conducted by the General Services Board of Contract Appeals (GSBCA), under GSBCA Rule of Procedure 204. The parties will participate in the selection of the arbitrator. (See 5 U.S.C. §577(a)). The arbitrator shall not have an official, financial or personal conflict of interest with respect to the issue in controversy, unless that interest is fully disclosed in writing and all parties agree that he/she may serve as the arbitrator. (See 5 U.S.C. §§573, 577(b)).

An arbitrator may regulate the course and conduct of the arbitration hearing. (See 5 U.S.C. §578(1)).

9. An arbitrator may administer oaths and affirmations. (See 5 U.S.C. §578(2)).
10. An arbitrator may compel the attendance of witnesses and production of evidence to the extent the IRS is otherwise authorized by law to do so. (See 5 U.S.C. §578(3)).
11. An arbitrator may make awards. (See 5 U.S.C. §578(4)).
12. The arbitrator shall set the time and place for the arbitration hearing and shall notify the parties of same at least five days before the hearing is to take place. (See 5 U.S.C. §579(a)).
13. Any party wishing a record of the hearing shall: (1) make the arrangements for it; (2) notify the arbitrator and other parties that a record is being prepared; (3) supply copies to the arbitrator and the other parties; and (4) pay all costs, unless

the parties have agreed to share the costs or the arbitrator determines that the costs should be apportioned. (See 5 U.S.C. §§579(b)(1)-(4)).

14. At any arbitration hearing, parties are entitled to be heard and present evidence material to the controversy, and to cross-examine witnesses appearing at the hearing. The arbitrator may, with the consent of the parties, conduct all or part of the hearing by telephone, television, computer, or other electronic means, if each party has an opportunity to participate. (See 5 U.S.C. §§579(c)(1) and (2)).
15. The arbitrator may receive any oral and documentary evidence that is not irrelevant, immaterial, unduly repetitious, or privileged. (See 5 U.S.C. §579(c)(4)).
16. The arbitrator shall interpret and apply any relevant statutes, regulations, legal precedents and policy directives. (See 5 U.S.C. §579(c)(5)).
17. No party shall knowingly have any unauthorized ex parte communication with the arbitrator unless the parties agree otherwise. If a party violates this provision, the arbitrator may require that party to show cause why the issue in controversy should not be resolved against it for the improper conduct. (See 5 U.S.C. §579(d)).
18. An arbitration award shall include a brief informal discussion of the factual and legal basis for the award. Formal findings of fact and law are not required. (See 5 U.S.C. §580(a)(1)).
19. A final award is binding on the parties and may be enforced pursuant to sections 9 through 13 of Title 9, U.S. Code. (See 5 U.S.C. §580(c)).
20. An arbitration award may not serve as an estoppel in any other proceeding and may not be used as precedent in any factually unrelated proceeding. (See 5 U.S.C. §580(d)).

II. Binding Arbitration Guidance'

A. Binding Arbitration: Description and Forms

After a final determination by the IRS, or the IRS and the Alliance, any member or new market entrant who has been refused the ability to list on the IRS Free File Website and any Alliance member who has been removed from the IRS Free File Website may challenge the determination to the General Services Board of Contract Appeals (GSBCA) in accordance with the GSBCA's Rule of Procedure 204. The GSBCA's review is authorized by the Alternative Dispute Resolution laws and regulations issued by the United States Government, and is in lieu of any litigation in any court. The GSBCA may either reject the member or new market entrant's challenge or direct the IRS, or the IRS and the Alliance, to list or relist the member or new market entrant on

the IRS Free File Website. The GSBCA may not offer any other relief, including attorney fees or other monetary awards of any kind. The GSBCA will be the exclusive venue for resolving disputes concerning any action taken by the IRS or the IRS and the Alliance under the terms of the MOU.

The member and/or new market entrant who challenges an IRS determination or a joint determination of the IRS and the Alliance shall not be entitled to any monetary remedies and the member's and/or new market entrant's sole and only remedy shall be an order directing the IRS, or the IRS and the Alliance, to act in accordance with the GSBCA's decision. The GSBCA's decision with respect to the termination or reinstatement of the member on the IRS Free File Website or any other order shall be final and binding on the IRS, the Alliance, and the member/new market entrant and shall not be subject to review.

B. Setting the Award "Cap"

There will be no monetary awards of any kind. A member or new market entrant's sole and only remedy shall be an order directing the IRS and the Alliance to act in accordance with the GSBCA's decision.

C. The Checklist of Arbitration Issues

Issue 1: For what types of cases will binding arbitration be used?

Response: Binding arbitration shall be available only to challenge a decision by the IRS, or by the IRS and the Alliance, that rejected an Alliance member's offering, removed an Alliance member's listing on irs.gov, or rejected an Alliance member's request that its listing be restored.

Issue 2: What type of awards will be made by the arbitrator?

Response: All awards will be non-monetary. The GSBCA may reject the member or new market entrant's challenge. If a challenge is successful, a member or new market entrant's sole and only remedy shall be an order directing the IRS, or the IRS and the Alliance, to act in accordance with the GSBCA's decision.

Issue 3: How and by whom will the decision to arbitrate be made?

Response: The decision to arbitrate is set forth in the MOU and the Alliance Operating Agreement.

Issue 4: Who will be the arbitrator?

Response: The IRS and the Alliance have agreed that the GSBCA will serve as the arbitrator.

Issue 5: Will the agency agree to allow non-attorneys to represent a party, or for a party to appear pro se at the arbitration?

Response: Yes.

Issue 6: How will the agency pay the arbitrator(s)?

Response: The Alliance shall be responsible for paying the GSBCA for all costs incurred by the GSBCA in any proceeding related to this provision. For the purposes of this section, a party to an adjudication may include any Member and the IRS or the IRS and the Alliance. A Member, or New Market Entrant who does not prevail in its appeal before the GSBCA is required to pay one hundred percent (100%) of the costs, fees and expenses incurred by the GSBCA and the Alliance. The Alliance will invoice the Member and/or New Market Entrant for such costs, fees and expenses and the Member and/or New Market Entrant shall pay the Alliance within ten (10) days of presentation of an invoice for such amount.

Issue 7: What must the arbitration award include?

Response: The arbitration award need not be in the form of formal findings of fact and conclusions of law, but must at least provide the factual and legal basis for the arbitrator's decision.

Issue 10: Will the agency allow arbitration on the documents only, without a hearing, or a telephonic hearing?

Response: The arbitrator, after consultation with the parties, will be authorized to render an award based solely on his/her review of the documents or based on telephonic testimony.