

**Thoughts on Achieving the Goal for E-filed Returns  
Remarks before the IRS Oversight Board by the  
Electronic Tax Advisory Committee (ETAAC)  
January 26, 2004**

Madame Chair, Members of the Oversight Board, and distinguished guests.

The Electronic Tax Administration Advisory Committee appreciates the opportunity to present our views. ETAAC membership includes representatives from a wide variety of IRS stakeholders, partners, and taxpayers, each of whom represents an important component of the overall plan for electronic tax filing goals.

This Advisory Committee was created as part of the Restructuring and Reform Act of 1998 (RRA 98) with the directive to provide information to Congress annually on the progress of IRS in meeting the RRA 98 goals, the status of the strategic plan to increase electronic filing, legislative changes necessary to assist IRS in accomplishing the goals, and the effects on businesses of electronically filing tax and information returns.

### **Status Report**

For the tax year 2002 there was an increase of over 12.5 % in the number of individual tax returns e-filed over tax year 2001. Although this represents a significant change, it indicates a trend toward lower adoption rates for the future than were experienced in the first years of e-filing. Business tax return e-filing levels remain low, and e-filing is not yet available for some business returns. It is not expected that the Internal Revenue Service will achieve the goal of 80% of all returns filed electronically by 2007.

Overall, it is clear that the low hanging fruit has been harvested. Early adopters who welcome new technology, enjoy change, and were enthusiastic about electronic filing are already on board. It will be a continuing challenge to convince those not currently e-filing that this should be the method of choice, for individuals, business e-filers, and third party bulk filers. We are entering a different phase of “selling” e-filing. Those waiting in the wings and watching the current programs are a different audience than those already converted.

### **Individual 1040 Returns**

The IRS has access to a wealth of statistical data with which to make marketing decisions. Barriers to adoption for the individual taxpayer have included the following themes: lack of awareness of e-filing and the associated benefits, lack of technology, fear or reluctance to change, security concerns, and privacy issues.

Although there have been surveys on taxpayer reasoning, in our 2003 Report to Congress ETAAC indicated that now is the time to dig deeper into these fairly global selections offered to surveyed taxpayers for their failure to move to e-filing. We think that more

targeted marketing strategies for the individual taxpayer will pay off once market segments are more clearly defined.

One-on-one interviewing or differently designed focus groups would be better vehicles for obtaining useful data on taxpayer reluctance to move to electronic filing. In fact, a one-on-one interview in which the interviewer can do specific follow-up would be the best vehicle to drill down on the root reasons for failure to e-file. Focus groups do not tend to lend themselves to analysis at the level we believe is necessary, but a creatively designed approach might bear fruit.

For example, if a taxpayer is worried about the privacy of tax information, the interviewer should probe to determine exactly where this fear originates in order to better address the specific concern. Privacy is a huge umbrella, and could range from concerns about inter-agency data sharing, generalized fears about identity theft, the threat of government maintaining a database on each individual, to a concern about the protection of private information from parties outside the government, or what amounts to more security concerns than privacy.

Another angle to consider is the 17 million paper returns filed from the taxpayer group that is labeled “self-prepared- simple”. These are returns prepared by the taxpayer (not a paid preparer) using form 1040EZ, 1040 or 1040 with no schedules.

A limited pilot program designed to tutor a small group of paper filers in e-filing should be conducted and evaluated in order to determine barriers to entry. The Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) programs provide assistance to more than 3 million taxpayers, 50% of which are using e-file. Access to computer and the internet is problematic at many VITA and TCE locations. The IRS should work with volunteer organizations that may provide technical assistance to these locations, as well as partner with other groups to reach those who do not have home use of the technology or in some cases, the aptitude to make use of it. Partnering with high schools, vocational institutions, and colleges would be another method of instilling the concept in the next generation that e-filing as the best way to file tax returns.

Marketing for e-filing to individuals continues to emphasize speedy refunds as the primary incentive for using e-file. While this may be the case during peak filing season, e-filed refunds are not dramatically quicker in the early part of the tax season. There still remains a fairly high number of refund returns filed on paper, so there are other legitimate taxpayer reasons for continued use of paper.

Up till now, there has not been a marketing approach that addresses those taxpayers who are either a zero balance return, or a payment due return. These individuals have not yet been presented with a compelling reason to seek e-filing. Marketing real life solutions that can address these populations is clearly needed.

Third party practitioners continue to be critically important in assisting IRS to meet its e-file goals. Barriers to adoption that third parties have indicated include; lack of a

compelling business case for changing from paper to e-filing, lack of parity in treatment between paper and e-filed returns, and reluctance to change business practices and/or technology.

In order to encourage a preparer to change their business practice, IRS must be able to articulate good business reasons for doing so. Many tax practitioners have satisfied clients, provide an excellent service to them, and see no reason to re-tool their methods or go through a conversion.

IRS has spent much effort trying to increase the market penetration of paid preparers. However, no one can deny that any conversion from already established methods/programs takes time and effort, and causes disruption, no matter how well planned and implemented.

We believe that IRS needs to concentrate on using those already converted to e-filing to sell this to others in their field. This includes CPAs, as well as all other Circular 230 and non-230 entities. A peer to peer message delivered by those who have successfully implemented such a change would be more effective than generic marketing from IRS. The pragmatic theme of “Why E-filing is Good for *My* Business”, presented by credible role models could be very powerful.

E-services for third parties are practical and cost effective incentives to offer practitioners. These services can be a win-win situation, since the IRS would gain processing efficiencies and reduce costs while the practitioner gains an enhanced ability to resolve and track client returns and accounts.

ETAAC has endorsed the IRS position of allowing access to only those preparers who have made an effort to join the e-filing ranks, which is currently defined as those who e-file 100 or more returns. In order to maintain momentum, it is paramount that IRS has the appropriate resources to fulfill previously published delivery dates for these and other services.

The following e-services are included in the IRS roll-out plans:

- 1.) The ability to submit a disclosure online
- 2.) Electronic Account Resolution
- 3.) Account transcript availability

Although e-services are attractive and useful, the mechanism for account resolution and transcripts will continue to remain available via the slower, current methods so this reason alone will not bring all practitioners into the fold.

There remains a lack of parity between paper and e-files returns for the tax practitioner. The required information for electronically filed returns is more stringent than on paper, and some error conditions that would be corrected at IRS service centers on paper returns are rejected back to the tax practitioner for correction, without tagging the return as initially timely filed.

In the paper world, the original postmark shows timely filing, even with some minor edit errors, and the processing center corrects or “perfects” the return, frequently without contacting the taxpayer. As long as tax professionals run the risk on non-timely filed returns that would have been timely filed on paper, many will continue to elect to stay with the paper option.

IRS should continue to explore positive ways to bring parity between paper and e-filing. The IRS should provide incentives for e-filing a high percentage of a tax practitioner’s returns, (not just the 100 to gain e-services) and accommodate conditional acceptance if e-filed returns fail some non- fatal screening criteria as is done with paper returns. IRS should also determine the impact of any future change to requirements on 1040s to make sure that they would be consistent with what the e-filing system can accommodate.

ETAAC also supports continued efforts on the part of Internal Revenue Service to partner with private industry to provide multiple avenues for free tax filing for low income taxpayers (such as the Free File Alliance) with appropriate oversight by the service. This partnering effort originated as a request from the Office of Management and Budget in 2001, and remains a cost effective method for IRS to gain more e-filers without having to maintain the infrastructure and software to do so in these times of competing resource requirements.

### **Business Tax Returns**

In the arena of business tax return e-filing, a totally different animal emerges from that of individual 1040 returns. First, there is no free method available for an individual business owner to e-file and second, there are few, if any, incentives for individual business taxpayers to switch to e-filing. This can be demonstrated by the fact that for tax year 2002, 81% of all Form 941, Employer’s Quarterly Federal Tax Returns were filed on paper.

Since 75% of Form 941s are zero balance due, and 10 % of 941s report zero wages, taxes, and deposits, IRS’ promotion of e-filing a payroll tax return essentially competes with a 37 cent stamp. There is no rapid refund benefit to promote.

Since this particular segment of e-filing is in its infancy, ETAAC believes that one of the first steps IRS should take is to partner with those companies filing multiple returns for clients by offering comparable e-services as are currently in the pipeline for 1040 practitioners. These e-services could lower government operating costs by allowing authorized self-service, which should increase the adoption rate of e-filing overall for employment tax returns.

A second step would be to research what would be compelling reasons to business owners to move to e-filing. Clearly the message to a business owner, as with a third party filer, would have to be why such a change is good for business, cost effective, or more efficient.

## **State Mandates**

While ETAAC has not come to any formal conclusions on the effect of state mandates on federal e-filing, there have been preliminary discussions on areas that should be considered in this environment in order to best serve the taxpayer. Some of these include: the need to encourage consistency amongst states while respecting the unique regulatory and system environments of each entity, recognition of practitioner and software developer concerns, and last but not least; clear communication of mandates, (how to comply, what options are available) to the taxpaying public.

## **Closing Comments**

As a final note, it is interesting that ETAAC members recently were given a presentation on the projected programs and systems to address the assumed residual paper returns.

It might be worthwhile to re-examine the thought processes that allow what we perceive to be a resignation to significant residual paper processing. This thinking permits a certain level of distraction from the main goal, and a clear siphoning of needed resources, time, money, intellectual capital, and human, so as to immediately start working on the programs to support this anticipated leftover paper processing.

Again, identifying why there is expected to be so much paper, then addressing those reasons in the current e-filing world would represent a less segmented approach. Not many businesses can survive supporting multiple processing pipelines, so it is not logical to think that IRS can easily do so as well. E-filing is the future, and keeping our eye on the target in this time of limited resources is essential.

This concludes our remarks to the Oversight Board. The ETAAC members would like to thank you for the opportunity to offer our comments on achieving the goal for e-filed returns.