



Consumer Federation of America



**Consumers
Union**

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The Honorable Charles Grassley
Chairman
Senate Finance Committee
United States Senate
Washington, DC 20510

The Honorable Max Baucus
Ranking Member
Senate Finance Committee
United States Senate
Washington, DC 20510

Dear Senators Grassley and Baucus:

We write to add our support to the efforts your committee has undertaken in recent weeks to protect the interests of American taxpayers when they file their tax returns. We agree with your concerns about: (1) the privacy issues raised by the IRS' proposed changes to regulations in order to permit commercial tax preparers to share or sell tax return information with third parties for marketing purposes, (2) the serious problems with the Free File agreement between the IRS and commercial software companies, and (3) the requirement that taxpayers pay private companies in order to electronically file their tax returns with the IRS. We believe your committee has done important work on consumer taxpayer issues, including holding a hearing investigating these issues as well as the accuracy and quality of commercial tax return preparation.

As you know, our organizations have advocated for several years to better protect consumers in their roles as taxpayers when doing business with commercial tax preparation companies and their partner banks. We submitted comments calling on the IRS to drop its proposed rules allowing sharing and selling of taxpayer information to third party marketers and data brokers. We have long taken the position that taxpayers should have the ability to electronically file their returns directly with the IRS without the need to pay or use a third party intermediary. We came out in support of S. 2550, a bill that calls for free electronic tax return filing and in opposition to H.R. 5114, the bill that protects commercial software and tax preparation companies by forbidding the IRS to offer direct electronic filing except through the Free File Alliance run by a private business consortium.

Privacy of Tax Return Information

Consumer and privacy groups, along with most of the state Attorneys General, filed comments opposing the proposed privacy rule changes heard by the IRS on April 4. The marketing, data mining or other commercial uses of tax return information expose consumers to security risks, identity theft, and intrusive marketing, not to mention a completely unwarranted invasion of their privacy. Our system depends on the

willingness of taxpayers to provide detailed personal financial information to the federal government in order to ensure accurate payment of taxes, the lifeblood of government. Erosion of public confidence in the security and privacy of that information undercuts the pact between taxpayers and their government to keep this information safe and confidential, and used only for the purposes of tax return preparation and tax collection.

Indeed, taxpayer return information is so sensitive that it should never be shared, sold, traded, or used for secondary purposes, including to cross-market ancillary products by any company, especially considering the great amount of trust that taxpayers have in their preparers and the potential for exploitation of that trust. Tax preparers should be prohibited from using tax return information to market their own products, and from sharing tax information with their affiliate companies as well as with third parties.

Free File Alliance Poor Deal for Taxpayers

We applaud your letter of April 13 to IRS Commissioner Everson cataloging the many problems Finance Committee staff identified with Free File company sites. As you discovered, and as Taxpayer Advocate Nina Olsen testified on April 4, the Free File sites are riddled with high cost extra products and services that are hard to avoid, failed to provide accurate tax preparation in all tested scenarios, and were only available to consumers with incomes below \$50,000. We are not surprised that Free File use dropped 20% this year. Many of our organizations filed comments opposing the original Free File agreement and subsequently raised issues with Treasury about privacy problems and marketing of refund anticipation loans with the implied endorsement of the IRS.

IRS Should Provide Direct Free Electronic Filing

While the short-term solution is for Commissioner Everson to renegotiate the Free File contract, the longer term solution is to make it possible for taxpayers to use tax return templates on the IRS web site to prepare and electronically file their own tax returns for free without going through a third party intermediary. We emphasize that permitting direct e-filing by consumers who have prepared their own tax returns using templates available on the IRS web site or using commercial software programs is not the same as “letting the IRS prepare your taxes.” Conflating these two concepts is deliberate obfuscation by those who wish to preserve the complete control of commercial preparers over electronic filing.

Direct and free electronic tax return filing with the IRS has many benefits for consumers:

- Taxpayers with simple returns could complete tax forms posted at IRS.gov and file directly. This would put electronic filers on the same footing as taxpayers who prepare returns on paper and mail in the completed returns and payment.
- Electronic forms would reduce math errors and mistakes that often occur with paper returns, saving both IRS and taxpayers time and extra work.

- Taxpayer information, including Social Security numbers, bank account information, and all the other intensely personal data on tax returns, would not be used by commercial tax preparers to market their affiliate company products and services and would not be shared or sold to third party companies for any reason. Direct filing strengthens privacy protections under current rules and especially under the proposed changes to IRS information-sharing regulations.
- Electronic filing by a larger proportion of taxpayers would improve efficiency for the IRS and speed up refunds to consumers, especially if they provide their bank account numbers for direct deposit from the IRS.
- Faster electronic filing and no marketing of high cost refund anticipation loans (RALs) will speed refunds to consumers and eliminate triple-digit interest rate loans that skim over \$1 billion from Earned Income Tax Credit benefits and over-withholding by the working poor who took out 12 million RALs last year.

It is hard to fathom why taxpayers in the United States get such poor service when they file their tax returns as required by law. For many years, Americans have been able to apply for federal student financial aid on www.fafsa.ed.gov and for Social Security benefits at www.ssa.gov. Many states make it possible for citizens to file state tax returns electronically for free. A free direct electronic filing program at www.irs.gov is long overdue. Instead, this year the IRS even discontinued its Telefile program, used by over three million taxpayers in 2005 to file their simple tax returns for free by calling the IRS with the necessary information.

Thus our organizations announced support of S. 2550, which would require the IRS to establish free electronic filing directly with the IRS via the Internet. We hope you will consider also supporting this bill or a similar measure.

Hart-Eshoo Bill Stifles Innovation and Service

We are dismayed that so many members of Congress have joined in sponsoring H.R. 5114, the so-called “Tax Return Choice Act of 2006.” This bill forbids the IRS from developing or providing taxpayers with free individual tax electronic preparation and filing services *except* through the private companies of the Free File Alliance or through only the Tax Counseling for the Elderly or VITA sites. The bill also repeals current law that requires the Secretary of the Treasury to develop procedures for the implementation of a return-free tax system beginning after 2007.

The implications of the Hart-Eshoo bill are far-reaching. It precludes new IRS services the year after Hurricane Katrina showed that new taxpayer service approaches are essential. The bill would evidently outlaw mobile tax units. Free Telefile services would never be permitted. No other free filing arrangement could be implemented.

The Hart-Eshoo bill stands in direct contrast with the taxpayer/consumer-friendly provisions of S. 2550. Should there be any companion bill to H.R. 5114, we urge you to reject it.

If you have any questions or need further information, please contact Jean Ann Fox, Consumer Federation of America, at 757-867-7523 or Chi Chi Wu, National Consumer Law Center, at 617-542-8010.

Sincerely,

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