



U.S. SENATE COMMITTEE ON

Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

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Grassley Exposes Key Tax Season Consumer Issues

WASHINGTON – Sen. Chuck Grassley, chairman of the Committee on Finance, today urged taxpayers to be careful using paid preparers to do their taxes and to look carefully at how much charities really benefit from vehicle donation. Grassley's comments came after he released new analyses showing consumer pitfalls in these areas.

“Today's findings are surprising,” Grassley said. “I think most of us figure we'll get the best possible financial outcome by having professionals do our taxes than by doing them ourselves. It's counterintuitive that professionals actually could make us worse off. And it's surprising that charities sometimes get pennies on the dollar from vehicle donations. With all of the ads encouraging vehicle donation, reasonable consumers assume charities always get the lion's share from those transactions. Unfortunately, that's not the case.”

Grassley convened a hearing of the Finance Committee, which has jurisdiction over the Internal Revenue Service, to examine these consumer issues in the midst of the tax filing season. Today's testimony from the General Accounting Office (GAO), the investigative arm of Congress, was a preview of two final reports to come in the next several weeks. Highlights of the GAO's testimony include the following:

On using paid preparers. The GAO reports that in tax year 2000, more than half of the 130 million individual filers paid someone to prepare their tax return. Taxpayers paid an estimated \$14.7 billion for this service. While many taxpayers were satisfied with the service they received, a significant number were harmed by paid preparers' mistakes.

Last year, the GAO estimated that more than two million taxpayers overpaid their 1998 taxes by \$945 million because they claimed the standard deduction when it would have been more beneficial to itemize. Half of these taxpayers used a paid preparer. The GAO said taxpayers likely contributed to some of the errors, but the findings raise questions about the extent of errors caused by paid preparers.

Even if a small percentage of taxpayers experience bad advice from paid preparers, that can affect millions of taxpayers, the GAO said. Those taxpayers may face significant consequences. They may overpay their taxes, overpay their preparers, or underpay their taxes and be subject to penalties

and interest.

For example, a paid preparer told the GAO of a disabled taxpayer with limited English skills who overpaid his taxes by about \$3,000 to \$5,000. The taxpayer had received notices for several years from the IRS stating he might be eligible for the earned income tax credit, a benefit for low-income individuals. Each year, he took the notices to his preparer but the preparer took no action. Eventually, he changed preparers, and his new preparer is working to amend his returns.

“This case is really upsetting, and I hope it’s atypical,” Grassley said. “Here’s someone who’s trying to comply with the law and file his taxes, and paying for professional help, and getting nothing in return but a bite out of his bank account.

“It’s shocking that paid preparers sometimes make very basic mistakes, like not advising folks to itemize instead of claiming the standard deduction. That seems like Tax Prep 101. Clearly taxpayers need to have their eyes open when choosing a tax preparer. And the IRS needs to increase its focus on the bad apple tax preparers as well.”

On donating vehicles to charity. For the tax year 2000, 733,000 people filed a tax return stating that they had donated a vehicle, according to the GAO. The taxpayers claimed deductions of an estimated \$2.5 billion for these cars and lowered their income tax liability by an estimated \$654 million that year. The GAO raised several concerns about charitable donations of cars:

Whether some taxpayers are overstating the value of their cars. The IRS limits the amount of an allowable deduction to a car’s fair market value. The GAO took a sample and didn’t have enough information about the cars’ condition and mileage to be able to determine whether the taxpayers were claiming values that reflected the cars’ fair market value.

Whether the taxpayers are contributing their cars to qualified organizations. Of a sample of 22 charities that the GAO submitted to the IRS, the IRS was able to verify that only 10 of the charities were qualified to receive tax-deductible donations.

Whether charities are seeing the lion’s share of the benefits from vehicle donation. The GAO reports that the proceeds a charity receives from a vehicle donation may be less than what a donor expects. An outside fund-raiser who solicits the donation may take a significant cut. And the charities and fund-raisers often sell the vehicles at auto auctions for wholesale prices or to salvage yards for parts, making less money than if the cars were sold to private parties.

In one case, a taxpayer in 2001 donated a 1983 truck to a charity whose vehicle donation program was operated through a fund-raiser. The gross sale price for the truck sold at auction was \$375. After fund-raising and advertising expenses were deducted, the charity received \$31.50 from the vehicle donation. The donor claimed a deduction of \$2,400 on his or her tax return.

Whether ads promoting vehicle donation are misleading. A majority of the ads the GAO reviewed don’t specify that taxpayers have to itemize to claim a vehicle deduction. This is misleading, because many taxpayers don’t itemize.

“These questions are troubling. We need to make sure Uncle Sam isn’t being taken for a ride by people overstating the value of their donated cars,” Grassley said. “And taxpayers should know that charities sometimes benefit very little from their generosity.”

Grassley said he plans to follow up with the IRS on these issues. In the meantime, he urged taxpayers to abide by the following tips compiled by the GAO:

On Choosing a Paid Preparer

When searching for a preparer, get recommendations from friends, co-workers, or other trusted people. Find out if you qualify for free services.

Interview the preparer before hiring to check out qualifications, experience, discipline problems, and any history of complaints.

Be sure you understand other services you will be getting, such as electronic filing or Refund Anticipation Loans. Find out whether these services are optional, what they will cost, and how they will benefit you.

Don’t hire a preparer who guarantees a refund before seeing your tax documents or whose fee is a percentage of your refund.

Make sure your preparer understands your personal circumstances, income, and expenses. Show your official tax documents to your preparer, including W-2s and 1099s.

Review your completed return before you sign it. Check that your tax information is correct. Even though someone else completed it, you are responsible for the accuracy of every item on your return.

Don’t sign a blank return and don’t sign in pencil.

Make sure your preparer’s signature and tax identification number are on the return before you submit it. Keep a copy of the final return.

Don’t make checks for taxes due payable to preparers. Checks should be made payable to the United States Treasury.

On Donating a Vehicle to Charity

Verify that the recipient organization is a tax-exempt charity. Potential donors can search IRS’ Publication 78, which is an annual cumulative list of most organizations that are qualified to receive deductible contributions.

Determine whether the charity is properly registered with the state government agency that regulates

charities. The state regulatory agency is generally the state attorney general's office or the secretary of state.

Ask questions about how the donated vehicle will be used to determine whether it will be used as intended. Such questions include the following: Will the vehicle be fixed up and given to the needy? Will it be resold, and if so, what share of the proceeds will the charity receive?

Itemize deductions in order to receive a tax benefit from the donation. The decision to itemize is determined by whether total itemized deductions are greater than the standard deduction.

Deduct only the fair market value of the vehicle. The fair market value takes into account many factors, including the vehicle's condition, and can be substantially different from the blue book value. IRS Publication 526, "Charitable Deductions," and IRS Publication 561, "Determining the Value of Donated Property," provide instructions on how to calculate the fair market value of donated property.

Document the charitable contribution deduction. IRS Publication 526 identifies requirements for the types of receipts taxpayers must obtain and the forms they must file.

Follow state law regarding the car title and license plates. Generally, the donor should ensure that the title of the vehicle is transferred to the charity's name, by contacting the state department of motor vehicles, and keep a copy of the title transfer. Donors are also advised to remove the license plates, if allowed by the state.