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Opening Statement of Senator Chuck Grassley
Hearing, “Filing Your Taxes: An Ounce of Prevention is Worth a Pound of Cure”
Thursday, April 12, 2007

I would like to start out by thanking Chairman Baucus for calling this hearing to examine the issues affecting the current filing season and to look at the roles and responsibilities of the tax preparation community.

The only thing that I would have changed about this hearing if I were still the chairman of this Committee would have been the title. I would have called it, “Sharks in the Water – Let the Taxpayer Beware,” because there seems to be an increasing amount of danger in receiving an inaccurate or even fraudulently prepared tax return.

In 2006, over 62 percent of all individual taxpayers used a paid preparer to complete their tax return. As a result, these preparers have a direct and substantial impact on tax compliance. And while I believe most tax return preparers are honest, knowledgeable individuals who serve the community well in providing sound financial advice, there are clearly some sharks lurking in the water. And these sharks are preying on innocent taxpayers – either through bad advice, incompetence, or downright fraud.

The first example that comes to my mind is the recent allegations against the Jackson Hewitt franchises. These allegations are very disturbing, considering that Jackson Hewitt is the nation’s second-largest tax preparation firm.

Examples of fraud alleged in the April 3, 2007, Jackson Hewitt civil injunction cases include filing false returns claiming refunds based on phony W-2 forms; using fabricated businesses and business expenses on returns to claim bogus deductions; claiming fuel tax credits in absurd amounts for customers clearly not entitled to any credits; and massive fraud related to claiming the federal earned income tax credit.

While it is great news that the IRS and the Department of Justice are working to close down these allegedly fraudulent tax preparation shops, it would have been better – in terms of protecting more taxpayers and producing a chilling effect on fraud – if the bolts were put on the doors earlier in the filing season. As it was, by the time that the Department of Justice filed suit, there were only two weeks left in the filing season.

Last year’s undercover investigation of paid preparers conducted by the Government Accountability Office (GAO) at the request of this Committee serves as yet another example of just how dangerous the tax preparation waters can be – and it also seems to indicate that the lifeguard is asleep on his chair.

In that investigation, the GAO found that out of the nineteen paid preparers investigated, not one properly prepared a tax return. Among the most serious problems that the GAO found involved paid tax preparers not reporting side income in 10 of 19 cases. Even in cases where the side income was reported, several paid preparers advised the GAO undercover investigators that reporting such

income was voluntary because the IRS would not know of it unless it was reported on the return. This type of inaccurate advice can hardly be attributed to the complexity of the tax code.

Yet, despite the GAO turning over the results of the investigation to the IRS, almost a year later the IRS has yet to complete a single audit on a single tax return filed by any of those nineteen preparers – and the IRS has not assessed preparer penalties on even one of those nineteen preparers in response to the GAO investigation.

In the meantime, hundreds, if not thousands, of innocent taxpayers unwittingly bring their most private financial information in to these same paid preparers every day. And these preparers, who gave inaccurate, if not intentionally fraudulent advice – and who have seen absolutely no repercussions from the IRS whatsoever, continue preparing tax returns – probably still giving the same bad advice.

The IRS and the Department of Justice need to pick up the pace on preparer cases. The IRS is moving at such a snail's pace on the GAO work that it appears as though they are not moving at all. This is not sending the right message to the paid preparer community. Paid preparers need to know that they will be held accountable. And the IRS and the Department of Justice need to be more proactive in getting that message across.

Another area that needs some proactive attention from the IRS is the filing of false tax returns using stolen identities. Identity theft is one of the fastest-growing crimes in the United States, and it is increasingly being used in the filing of false returns. Yet, the IRS has no systematic way of identifying cases involving claims of identity theft or what the impact of these cases are in terms of the aggregate dollar value of refunds issued. Resolution of cases involving identity theft can be time-consuming, frustrating and difficult for the victims – especially when the IRS is not reaching out to help the taxpayers who fall victim, but is instead interrogating them as though they were the crooks.

We in Congress need to do more to ensure that those who are preparing returns possess the competence and ethical standards necessary to maintain the integrity of our tax system. Last year, this committee passed a bill that would regulate paid preparers and provide better taxpayer protection and assistance, but it didn't get brought up for a full Senate vote. We need to look at getting a similar bill passed this year.

And while I understand that no amount of regulation is going to prevent outright fraud, it is essential that the IRS impose stringent oversight of the paid tax preparation community and, where applicable, impose penalties and prevent the practitioner from preparing returns and representing taxpayers before the IRS.

In looking at this bill, we need to consider whether the law as it stands today provides adequate protection to victims of identity theft whose information is used in the filing of false tax returns and what can be done better to assist these taxpayers in resolving their cases with the IRS.

And we need to consider whether the IRS is fulfilling its obligation to help taxpayers understand and comply with their tax obligations. In looking at this, we need to determine whether the free electronic filing methods that exist today are effective in assisting taxpayers to determine their correct tax liability – and if they are not, we need to determine what the proper role of the IRS should be in ensuring that such a method exists.