



U.S. SENATE COMMITTEE ON

# Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

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Hearing, "Preparing Your Taxes: How Costly Is It?"  
Statement of Sen. Chuck Grassley  
Tuesday, April 4, 2006

In today's hearing we will examine the current state of tax preparation and electronic filing services. We will also look at how states are succeeding in the area of electronic filing. Twenty states plus the District of Columbia now offer direct Internet filing through state-sponsored websites. State electronic filing has consistently grown at a faster rate than federal electronic filing. In 2005, five states actually received more electronic returns than the federal government received from those states. With so many people using paid preparers and electronic filing systems, we need to ensure that these preparation methods are helpful and user-friendly for American taxpayers. The feedback we are receiving is that the tax preparation system is severely breaking down. In this hearing, we will look at some bad practices that seem to be pervasive and systemic in the industry. This hearing should be a call to action for this committee and the Congress. Given the complexity of our current system, taxpayers should be entitled to a tax preparation method that they can trust and rely upon.

Today, more than 60 percent of all returns are completed by paid preparers. This means that the paid preparer community annually prepares more than 78 million individual tax returns. While I believe that the large majority of tax return preparers are honest, highly-educated individuals who serve the community well in providing sound financial advice, we are getting reports that an increasing minority is doing a disservice to the American public — some through bad advice, some through incompetence, and some through taking advantage of the public by unscrupulous means.

Adequate training within the paid preparer community is essential. And for any practitioner who is not abiding by the tax laws, the IRS needs to impose penalties, and prevent that practitioner from preparing returns and representing taxpayers before the IRS. Today, any Joe can hang a shingle and prepare income tax returns — there are no requirements at all. It's incredible that we have legal requirements for someone to qualify as a barber to cut your hair, and yet there are no requirements for someone to prepare your taxes. The worst that can happen when you get a lousy barber is you have a bad hair day. But if you get an unqualified tax preparer who gives you bad advice, you may be audited, owe thousands of dollars, and even face jail time.

The vast majority of Americans want to do the right thing and pay their taxes. Americans have a right to expect that when they hire a tax preparer they are going to get honest, straightforward advice — but as we saw on NBC News last night, and as we will learn from the testimony of the Government Accountability Office today — too often that isn't the case.

Mr. Brostek and his investigative associates from the GAO will testify about their experience in reviewing the practices of tax preparers on an undercover basis. The results of that investigation, which will be outlined by GAO today in more detail, are very troubling.

The GAO visited 19 offices of national tax return preparers in a single major metropolitan area. More than half of those preparers declined to include cash income that was disclosed by the GAO investigator on the tax return. When the return involved the earned income credit, nine out of ten preparers initially left the cash income off of the return and eight out of ten claimed child-related benefits for children who did not live with the taxpayer during the tax year. One of these preparers redid the return upon request of the GAO investigator, but not without charging more than two times the upfront cost estimate.

For those taxpayers who can prepare their own returns, they should be able to do so electronically without cost. To achieve that goal, Congress allowed the IRS to establish the Free File program in 2002. We are reviewing the operations of the Free File program and have asked the Taxpayer Advocate to do the same and comment on their findings as part of today's hearing.

Here is some of what we know from our internal staff review. For the 2004 tax year, the Free File Alliance offered free filing services to everyone – without restriction. For the 2005 tax year, the new Free File Agreement signed by the IRS restricted the availability of Free File by placing income restrictions on the program. Not surprisingly, IRS statistics show that use of the program has decreased more than 21 percent from the same time last year.

Finance Committee staff found that many of the Free File companies place restrictions on the types of income and deductions taxpayers may claim using their free online tax preparation services. Also, taxpayers are being inundated with additional charges that may accrue and the sale of ancillary services. Such charges include fees for state return preparation and filing, resetting passwords, printing and mailing services, professional tax return review, audit protection, live chat help, telephone technical support, per-question fees for consultation with a tax professional, and vault service.

Taxpayers entitled to a refund from the government receive offers for anticipation loans, to have fees deducted from their refunds, or offers to get their refunds by cashier's check, prepaid Visa card, or retail gift card – all with hidden costs to the taxpayer. One free file site even contains a link where the taxpayer can sign up for a tax preparation franchise – no experience necessary – all for the low cost of \$15,500. Meanwhile, H&R Block, the nation's largest tax preparer, is being charged with breaching its fiduciary duty to customers by using a sales force of inadequately trained tax preparers to sell them IRAs and provide financial counseling services.

The lawsuit filed by the New York Attorney General accuses H&R Block of failing to disclose important information about fees and commissions, failing to provide individualized analysis of customers' financial needs, and pressuring customers, many of whom were unsophisticated in financial matters, into making quick decisions to invest in IRAs. This lawsuit comes on the back of a settlement by H&R Block in December for nondisclosure of fees relating to refund anticipation loans. To help us examine these issues, we benefit from the testimony of Michael Brostek, Director of the Strategic Issues Team at GAO; Bert DuMars, Director of Electronic Tax Administration at the IRS; Nina Olson, the Taxpayer Advocate; Robert Weinberger, Vice President of Government Relations at H&R Block, here today as a Member of the Free File Alliance; Francis Degen, President of the National Association of Enrolled Agents; and Harley Duncan, Executive Director, Federation of Tax Administrators.