



Consumer Federation of America



**Consumers  
Union**  
Nonprofit Publisher  
of Consumer Reports

October 5, 2005

Mark W. Everson  
Commissioner  
Internal Revenue Service  
Department of the Treasury  
1111 Constitution Ave., NW  
Washington, DC 20224

Eric Solomon  
Assistant Secretary  
for Tax Policy (acting)  
Department of the Treasury  
1500 Pennsylvania Ave., NW  
Washington, DC 20220

Dear Commissioner Everson and Assistant Secretary Solomon:

We are writing to express our concerns with recent Free File memos issued by SPEC (Attachments 1 and 2), which state that VITA volunteers may not negatively promote RALs to taxpayers, in essence a “gag rule” on anti-RAL efforts. While we understand these particular documents have been rescinded, we are extremely troubled that they were ever issued in the first place. Furthermore, we have no assurances that a similar directive will not be issued in the future, especially given that it was based upon the idea that VITA volunteers represent the IRS and are an extension of the IRS, and the IRS cannot promote one product over another (see Question 6 of Attachment 2 “Free File Questions and Answers”).

This now-rescinded gag rule reinforces our criticism of the IRS’s permitting RAL marketing in the Free File program in general, a subject that we have previously written about (see Attachment 3). Apparently, someone in IRS was highly concerned that even non-IRS employee *volunteers* warning taxpayers about the predatory nature of RALs would violate this IRS prohibition against promoting one product over another. Yet the IRS website [www.irs.gov](http://www.irs.gov) specifically directs taxpayers to the websites of certain commercial tax preparation companies, who then freely promote RALs to taxpayers, creating the appearance of a government endorsement. There appears to be a significant double standard here.

We object to any IRS directive or policy that would restrict the free speech rights of volunteers and VITA programs to warn or educate taxpayers about the predatory nature of RALs. We request that the IRS officially respond that it will not prevent any VITA program from allowing its volunteers or staff to educate taxpayers about RALs and other tax related financial products.

Finally, the Free File FAQ memo mentions that the agreement between the IRS and the Free File Alliance ended in April 2005. We strongly urge the IRS in re-negotiating the new agreement to prohibit the marketing of RALs and other ancillary financial products to Free File taxpayers. We also request that a consumer representative be included in the negotiations to the Free File agreement.

If you have any questions about this letter, please contact Chi Chi Wu at 617-542-8010. We would very much appreciate the opportunity to meet with you or Free File officials concerning the issues raised in this letter.

Sincerely,

Chi Chi Wu  
National Consumer Law Center  
(on behalf of its low-income clients)

Jean Ann Fox  
Consumer Federation of America

Gail Hillebrand  
Consumers Union of U.S., Inc.

Ed Mierzwinski  
U.S. Public Interest Research Group (U.S. PIRG)

cc: Nina Olson, National Taxpayer Advocate  
Rich Morgante, Commissioner Wage & Investment, IRS

Attachment 1

# TALKING POINTS for MANAGERS

## *Use of Free File Products by VRPP*

### Key Messages:

- **Volunteer sites may use the online commercial tax preparation products offered through Free File.**
- **VRPP volunteers may not recommend or endorse any one Free File product or company over another.**
- **VRPP volunteers may not promote (positively or negatively) the use of pre-refund loan products, such as a RAL (Refund Anticipation Loans).**
- **VRPP volunteers may not prepare the taxpayer's return using the Free File products.**
- **Volunteer sites using the products offered by the Free File Alliance do not qualify to receive IRS loaned equipment (computers or printers).**

### Background

Free File allows individual taxpayers to use online commercial tax preparation software to prepare and e-file their federal tax returns for free. These free services, offered by the Free File Alliance, LLC (not the IRS), are listed and accessible at [www.irs.gov](http://www.irs.gov).

Since its creation in 2003, SPEC Partners have used the products offered through the Free File Alliance to provide electronic tax preparation assistance to qualifying taxpayers. Until now, SPEC did not have a published policy regarding use of these products by the volunteer sites.

To ensure use of the products offered through Free File by SPEC's VRPP (Volunteer Return Preparation Program) complies with the IRS/Free File Alliance agreement, we requested guidance from the Electronic Tax Administration (ETA) and General Legal Services (GLS). The policy provided ensures SPEC's compliance with the agreement.

### Highlights

- Volunteer sites may use the online commercial tax preparation products offered through Free File.
- VRPP volunteers may inform (or demonstrate to) taxpayer's where/how to locate the Free File web pages within [www.irs.gov](http://www.irs.gov).
- VRPP volunteers may not recommend or endorse any one Free File product or company over another.
- VRPP volunteers may not direct taxpayers to Free File companies simply because the company supports a specific state e-filing program.
- VRPP volunteers may not promote (positively or negatively) the use of pre-refund loan products, such as a RAL (Refund Anticipation Loans).
- VRPP volunteers may not prepare the taxpayer's return using the Free File products.


## Support

- SPEC Territory Offices may provide support to sites using the products offered through the Free File Alliance
- SPEC Territory Offices may not provide equipment such as computers or printers

## Key Impact

- Partners who establish sites using the on-line commercial tax preparation products offered through Free File do not have the ability to capture production through use of the SIDN (Site Identification Number). The products provided through the Free File Alliance are for individual use. Since the taxpayer is assumed to prepare their own return using these products, there is no space provided in these products for capture preparer information, such as the SIDN.
- Quality – Quality may be impacted since the site volunteers are not trained in all products available to taxpayers through the Free File Alliance. Some partners may have recommended certain products based on familiarity in the past, however under the new agreement volunteers may not recommend or endorse one product over another.
- Fees for State Return Filing – All of the products offered through Free File provide free e-file of Federal tax returns; however, some of the products charge a fee for state return filing. VRPP offers free tax assistance. The inability to limit taxpayer's product choice to only those products offering free State return filing may cause customer dissatisfaction (e.g. sites not allowing taxpayers to use volunteer provided resources to prepare a State return when a fee is charged).

Attachment 2



## VRPP Free File Questions and Answers

- 1) **How should VRPP sites operate using the products provided through the Free File Alliance?** Sites can continue to use the on-line commercial products offered by the Free File Alliance to assist taxpayers preparing their return. Partners can provide computers with Internet access for taxpayers use; \*provide assistance establishing an email account for the taxpayer to receive their acknowledgement; and provide tax law assistance. Partners can not promote use of one product over another; discourage taxpayers use of a RAL; prepare the taxpayers return; and should not offer troubleshooting advice regarding use of the software product.
- 2) **Why won't the Free File Alliance modify the products to allow us to capture SIDN production?** The Alliance's targeted audience is individuals. It does not promote the use of the products offered through the Free File program for use by EROs. The products they provide are individual products and do not have the ability to capture the SIDN data.
- 3) **What are the options?** Partners may continue to use the Free File products as long as they adhere to the policy. Based on research provided as we considered this policy, most of the partners who were using the Free File products were doing so because they were using loaned equipment and did not have the ability to download a software program or maintain data on the computer. The new IRS/UTS contract provides a web-based product. No software will need to be loaded and no data will be stored on the user's computer. It is recommended that partners meeting the requirement to receive IRS provided software apply for an EFIN and use TaxWise web-based for FY2006.
- 4) **Can we provide equipment to volunteer sites using Free File products?** No. SPEC is constantly asked to prove return on investment (ROI) for the resources provided. Since we are unable to capture and verify production and statistical data for our partners using the Free File products, we cannot justify allowing use of IRS loaned equipment.
- 5) **What prompted the release of this policy?** The original agreement entered into by the IRS and the Free File Alliance ended April 2005. When negotiating the new agreement, SPEC's use of the products offered through the Alliance was mentioned. To provide support for this valuable program, SPEC agreed to [develop](#) a written policy in support of the agreement.
- 6) **Why can't partners promote products that provide free Federal and State preparation?** SPEC VRPP Partners represent the IRS. The IRS is prohibited from promoting one product's use over another. As an extension of the IRS, SPEC partners are also prohibited.
- 7) **Is there a concern over our taxpayers choosing a product that does not offer free State return preparation?** We have asked GLS to specifically address this issue and are awaiting their response. In the meantime, ETA provided the following guidance - VITA provides free Federal return preparation. Preparation of a State return is ancillary. If the guidance from GLS contradicts this opinion or causes greater restrictions on use of the Free File products by the volunteer sites, we may need to amend our policy. We will keep you informed.

*\*VRPP sites are not acting in the roles of Authorized e-file providers, Intermediate Service Providers, Transmitters or EROs and are not allowed to accept or monitor acceptance and rejection notices from Free File providers on behalf of the taxpayers. Taxpayers must have valid e-mail addresses and are responsible for monitoring acceptance or rejection.*

8/24/05

Attachment 3

**Consumer Federation of America**  
**1424 16<sup>th</sup> St. NW, Suite 604, Washington, DC 20036**  
**Consumers Union**  
**1666 Connecticut Avenue NW, Suite 310, Washington, DC 20009**  
**National Consumer Law Center**  
**77 Summer Street, 10<sup>th</sup> Floor, Boston, MA 02110**  
**U. S. Public Interest Research Group**  
**218 D Street SE, Washington, DC 20003**

September 4, 2002

Mr. Paul J. Mamo  
Internal Revenue Service  
1111 Constitution Avenue, Room 2403  
Washington, DC 20224

Re: "Electronic Tax Preparation and Filing; Intent to Enter Agreement"  
Federal Register August 8, 2002

Dear Mr. Mamo:

Consumer Federation of America, Consumers Union, the National Consumer Law Center (on behalf of its low-income clients), and U. S. Public Interest Research Group file these comments concerning the Internal Revenue Services' proposed Agreement to provide free services for online tax preparation and filing services.<sup>1</sup> The IRS has proposed to enter into an agreement with a Consortium of commercial companies to provide free online tax filing for up to 60 percent of taxpayers through a link from the IRS.gov website to the Consortium companies, instead of providing free e-filing capability directly from the government to taxpayers.

We believe that the proposed Agreement is seriously deficient and does not protect the interests of taxpayers, especially low-income taxpayers. Instead of entering into this Agreement, which is of limited benefit and exposes taxpayers to the risks of usurious tax refund loans, we urge the IRS to provide e-filing on its own website. We also urge the IRS to provide more free tax preparation services to low-income taxpayers. In the alternative, the IRS should amend this proposed Agreement to remedy the gaps described in this letter and to widen the circle of groups involved to include representatives to low-income taxpayers and consumer organizations.

### **The IRS Should Provide On-Line Filing on Its Own Website**

The Consortium project is offered as a substitute for the IRS providing free online tax preparation and filing capability directly to taxpayers. The IRS does not allow consumers to file their taxes on-line in an age where some state tax agencies allow taxpayers to file online (e.g. Massachusetts). In addition, consumers can file applications on-line with a number of other federal and state government agencies, such as the Social Security Administration (Social Security benefits), the Department of Education (college financial aid), and some state

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<sup>1</sup> 67 Fed. Reg. 51621 (August 8, 2002)

Department of Motor Vehicles (for replacement for drivers license). And of course, there are literally hundreds if not thousands of private entities that permit on-line filing.

Instead of providing on-line filing like other government agencies, the IRS has chosen to provide free on-line filings to only a portion of those it is supposed to serve. Furthermore, the IRS has chosen to meet this need by exposing taxpayers to the risks of costly ancillary services, such as refunds anticipation loans, fees for personal assistance, or padded prices for state tax return preparation services.

### **The Proposed Agreement is Unlikely to Provide Substantial Benefit To Low-Income Taxpayers**

This proposed Agreement is unlikely to benefit the working poor who now go to commercial tax preparers for help in filing for EITC benefits and other tax credits. The major obstacle for low-income taxpayers is not lack of free e-filing, but lack of free preparation for more complex EITC forms. The National Taxpayer Advocate's FY 2002 Report notes that only 113,000 of the 17 million low-income taxpayers eligible for the EITC in 1998 were served by free tax preparation services.<sup>2</sup> Furthermore, EITC-eligible taxpayers have the most need of tax preparation services, because of the complexity of the EITC forms and the limited education/literacy of this population.<sup>3</sup> Because there are so few free community tax preparation services, many of these low-income taxpayers are forced to turn to the often-expensive services of paid preparers. It is also the lack of free tax preparation services, combined with the fact that many of these consumers do not have the cash up front to pay for paid services, that forces them to take out RALs to finance the services.

The proposed Agreement will not help alleviate this problem for several reasons. As a preliminary matter, it is unclear whether both online tax preparation and electronic filing will be free to consumers who use the proposed Consortium service. The Federal Register notice states as an objective: "Seeking to assure access to a free and secure electronic preparation and filing option for additional taxpayers, building upon free electronic tax preparation and filing provided in the commercial market today."<sup>4</sup> This implies that both online tax preparation software and electronic filing will be free to consumers. However, the press release announcing this initiative from the Office of Management and Budget states "78 million will no longer have to pay to file their tax returns online. Currently, taxpayers who choose to file online can pay an average of \$12.50 in filing fees in addition to the cost of purchasing tax preparation software."<sup>5</sup> This implies that only free on-line filing will be available.

Even if the proposed Agreement does include free on-line tax preparation, there is no requirement that the Consortium serve the neediest of consumers. The proposed Agreement calls for each tax preparation company and software publisher in the Consortium to offer free services to at least 10 percent of the taxpayers each serves, but it does not specify which groups of taxpayers should receive free service. The proposed Agreement does not spell out who will be

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<sup>2</sup> National Taxpayer Advocate, FY 2001 Annual Report to Congress, December 31, 2001, at 51.

<sup>3</sup> Michael O'Connor, *Tax Preparation Services for Low Income Filers*, 90 Tax Notes 231, January 8, 2001.

<sup>4</sup> 67 Fed. Reg. at 51,621.

<sup>5</sup> Office of Management and Budget, Press release, July 31, 2002.

eligible for free online tax preparation versus only free electronic filing. There is no requirement that Earned Income Tax Credit recipients must be included in the 10% each company will serve or that EITC forms must be included in the online tax preparation service offered by all participating companies.

Moreover, the proposed Agreement will face the barrier of the digital divide for low-income taxpayers. Many taxpayers will be unable to take advantage of free online tax preparation or filing because of lack of Internet access. A recent report by the Electronic Tax Administration Advisory Committee acknowledges this fact.<sup>6</sup> Thus, even if the Agreement does include online preparation, that will do little good for many taxpayers, since 49% of households do not have Internet access at home.<sup>7</sup> Furthermore, approximately 46% of taxpayers do not use the Internet anywhere.<sup>8</sup> The situation is even worse for low-income taxpayers. Only 25% of taxpayers who earn under \$15,000 use the Internet.<sup>9</sup> Only 33% of the next income level, working poor taxpayers who make \$15,000 to \$25,000, use the Internet.<sup>10</sup>

Finally, the proposed Agreement does not address the lack of access to bank accounts needed to speed refunds. The ETAA Report notes that one of the incentives to encourage e-filing is expedited refunds.<sup>11</sup> To receive fast refunds when taxes are filed electronically, taxpayers must have a bank account into which refunds can be deposited. Yet, nowhere does the proposed Agreement or the ETAA Report consider the 10 million unbanked customers, many of whom are EITC recipients. Adding a Treasury-provided bank account to receive electronically delivered tax refunds would address this.

### **The Proposed Agreement Will Put More Taxpayers At Risk for Costly Services, such as Refund Anticipation Loans (RALs), Padded Fees for State Tax Return Preparation, and Fees for Personal Assistance.**

This proposed Agreement is unlikely to assist consumers without exposing many customers to high-priced ancillary products and services, such as refund anticipation loans (RALs). These are triple-digit interest small loans made by banks and currently marketed to low-income consumers through commercial tax preparation companies. These are high risk, high cost loans that bleed hundreds of millions from low-income taxpayers and the EITC program. The numerous problems with RALS have been documented by not only consumer groups, but the Brookings Institution.<sup>12</sup>

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<sup>6</sup> Electronic Tax Administration Advisory Committee, 2002 Report to Congress (June 30, 2002) (“ETAA Report”), at 11.

<sup>7</sup> U.S. Dep’t of Commerce, Econ. & Statistics Admin. and Nat’l Telecomm. & Info. Admin., A Nation Online: How Americans are Expanding Their Use of the Internet (Feb. 2002) at 5, [available at http://www.ntia.doc.gov](http://www.ntia.doc.gov).

<sup>8</sup> *Id.* at 8.

<sup>9</sup> *Id.* at 28.

<sup>10</sup> *Id.*

<sup>11</sup> ETAA Report at 2.

<sup>12</sup> Chi Chi Wu, Jean Ann Fox, and Elizabeth Renuart, “Tax Preparers Peddle High Priced Tax Refund Loans: Millions Skimmed from the Working Poor and the U. S. Treasury” Consumer Federation of America and National Consumer Law Center, January 31, 2002, available at [www.consumerlaw.org](http://www.consumerlaw.org); Alan Berube, et al., “The Price of Paying Taxes: How Tax Preparation and Refund Loan Fees Erode the Benefits of the EITC,” Brookings Institution and Progressive Policy Institute, May 2002, available at [www.brookings.org](http://www.brookings.org).

For those taxpayers who do have Internet access and use the proposed free services, they will become prime audiences for solicitations and advertisements for RALs. The IRS intends to provide a direct link on its website to commercial tax preparation companies, implying an endorsement of these companies, without sufficient safeguards to protect consumers. The IRS appears more interested in meeting the Congressional mandate for 80% electronic filing by 2007 than it is in serving the best interests of taxpayers who most need access to free tax preparation services and e-filing. Taxpayers need to be able receive their refunds and tax credits quickly without becoming trapped in usurious loans.

For years, IRS's e-filing program had the effect of encouraging the RAL industry. The proposed Agreement will drive even more taxpayers into the arms of paid preparers, where they will become a captive audience for refund anticipation loans. According to the ETAA Report, the IRS efforts are aimed at encouraging the 30 million taxpayers who now prepare their own returns by hand and file them on paper to file electronically using the proposed Consortium companies' "free" services.<sup>13</sup> These are taxpayers who currently do not pay commercial tax preparers to complete their returns and are unlikely to now be RAL customers.

How will Consortium members recoup lost revenue from providing "free" electronic tax filing for millions of taxpayers? The ETAA Report notes that "tax preparation companies may realize significant client development benefits from providing free Internet access in their offices."<sup>14</sup> Nothing in the proposed Agreement prevents commercial tax preparers from marking up or "padding" the price for preparing state tax returns. They are also free to charge fees for providing "personal" customer assistance to taxpayers who use the "free" service.

Some software companies already package RALs with their tax preparation programs.<sup>15</sup> Even taxpayers without Internet access will be at risk of RALs. It would be all too easy for the paid preparers, who make tens of millions of dollars from RALs, to encourage these taxpayers to "come into our office for free e-filing if you don't have Internet access." At the paid preparer's office, the taxpayer will be subject to a high-pressure, face-to-face sales pitch for RALs.

The proposed Agreement does not provide adequate protection against cross-marketing of high priced services or predatory small loans to consumers. The Federal Register notice merely notes that "Consortium Participants shall also agree that provisions of Free Services shall not be conditioned on obtaining an eligible taxpayer's consent to solicitations of additional business."<sup>16</sup> This provision simply prohibits tying of additional services to free tax filing. The IRS should go further to explicitly prohibit Consortium members from offering or selling RALs to taxpayers receiving free service, padding fees for other services, or charging for personal assistance.

## **Recommendations:**

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<sup>13</sup> ETAA Report at 2.

<sup>14</sup> *Id.* at 11.

<sup>15</sup> NCLC/CFA Report at 15.

<sup>16</sup> 67 Fed. Reg. at 51,622.

1. The IRS should scuttle the proposed Agreement with the Consortium and offer free electronic tax filing capability at the IRS web site directly. In addition, the IRS should provide more free tax preparation assistance for low and moderate income consumers, especially those who receive the Earned Income Tax Credit and other credits.
2. If the IRS proceeds with the proposed Agreement with the Consortium, it should provide unequivocally that paid preparers are forbidden to make or facilitate RALs to taxpayers who are being provided benefits under this program. There should be no extra charges for personal assistance. The price of also preparing state tax returns must be clearly disclosed and must not be “padded”.
3. EITC-eligible taxpayers must be included in the 10% of customers served by all Consortium members.
4. The IRS must make provisions in the Agreement to require preparers to provide bank account options to taxpayers without bank accounts. The Department of Treasury, which the IRS is a part of, has spent much effort to encourage unbanked consumers to open bank accounts. The IRS should get on this bandwagon and use the proposed program to encourage the same.
5. The IRS should ensure that taxpayers who don’t have a computer or Internet access will not be forced to go through a paid preparer, and will be served by this program through free community tax preparation programs.
6. The Consortium that will oversee this program should include taxpayer representatives.

Sincerely,

Jean Ann Fox  
Consumer Federation of America

Frank Torres  
Consumers Union

Chi Chi Wu  
National Consumer Law Center

Edmund Mierzwinski  
U. S. Public Interest Research Group