Electronic Tax Administration Advisory Committee

Annual Report to Congress

June 30, 1999

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Executive Summary

In 1998, the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 was enacted into law. This major legislation set a new direction for the IRS in many areas, including the establishment of a Congressional policy that paperless filing should be the preferred and most convenient means of filing Federal tax and information returns, and that the IRS have a goal that at least 80 percent of such returns be filed electronically by the year 2007. Additionally, the Act required that the IRS establish a private sector advisory committee to assist it in meeting these goals, and further required that the advisory group report to Congress annually on the IRS' progress. The Electronic Tax Administration Advisory Committee (ETAAC) is submitting this report to Congress in compliance with the Act.

The ETAAC has worked with the IRS since its establishment in September 1998. This report documents the advice the ETAAC has provided the IRS and identifies to Congress the major challenges, risks, and opportunities facing the IRS, as well as recommendations that the ETAAC believes the IRS should follow.

The IRS has made a good start in setting out a program to achieve the electronic filing goals established by Congress. Progress is evidenced by:

- Release of a strategic plan, *A Strategy for Growth*, in December 1998, which described IRS' approach for achieving its electronic tax administration goals.
- An increase of 19 percent in electronic filing during the 1999 tax filing season.
- Initiation of programs in 1999 designed to increase the attractiveness of electronic filing and the development of plans for additional initiatives for 2000 and future years.

Implementing *A Strategy for Growth* will challenge the IRS. Although the IRS has established a separate group responsible for electronic tax administration, the goal of achieving 80 percent electronic filing by 2007 is too sweeping in scope to be achieved by a single group within the IRS. The goal will only be achieved by placing responsibility for achieving ETA goals on each business unit as well as the ETA group. The plan established in *A Strategy for Growth* must be an agency-wide priority with application of the necessary resources throughout the agency. Continual progress evaluation and updating of the plan, with input from each of the business units, is essential.

The IRS Restructuring and Reform Act of 1998 requires that that the IRS strategic plan for electronic filing provide that, to the extent practicable, all information and tax returns prepared electronically should be filed electronically by the 2003 tax filing season. The ETAAC believes this to be an excellent strategy, but also believes that a broader set of initiatives or incentives than is currently planned will be necessary for the IRS to achieve this goal. Additional initiatives and incentives will likely be needed to meet the 2007 goal as well. In both cases, the broadest range of initiatives and incentives should be considered, including those that require legislative action.

The IRS faces a number of strategic challenges and opportunities while seeking to its electronic filing goals. The ETAAC believes these challenges are:
Business challenges

- Creating new processes and incentives for electronic tax administration that deliver value to all taxpayer segments (individuals, small businesses, large corporations, and tax-exempt organizations).
- Developing a strategy that provides strong incentives to all professional tax practitioners to enroll as EROs.
- Convincing taxpayers and professional tax preparers, through communications and marketing, that e-filing should be the filing method of choice.

Internal Management Challenges

- Transitioning to a customer-centric organization providing taxpayers with customer-segmented, tailored, and responsive products and services while concurrently transitioning to electronic services and systems and maintaining legacy systems that support paper filing.
- Integrating multiple agency-wide strategic plans, including *A Strategy for Growth*, the Modernization Blueprint, and the organizational modernization plan, into one cohesive business and strategic plan for the Service.
- Ensuring adequate resources are committed to the implementation of electronic tax administration projects and initiatives.
- Holding the executives of each new operating division accountable for achieving the electronic tax administration goals for the taxpayer segment assigned to the division.

Technology Challenges

- Implementing the necessary technology infrastructure to support the IRS electronic tax administration business goals, including security, privacy, database, and communications systems.
- Developing and maintaining the ability to receive electronically all the forms from all types of returns from all filers.
- Developing a scalable technology architecture that will support the growing volumes associated with achieving the electronic tax administration business goals.

A Strategy for Growth indicates that the IRS must position itself to take full advantage of the public's growing acceptance and use of the Internet. The ETAAC strongly endorses the formulation of an Internet strategy.

The ETAAC believes the IRS has opportunities to expand its business partnerships with professional preparers, large transmitters, software providers, payroll and tax processors, and state taxing agencies, as well as expand its relationship with the taxpaying public and businesses.

The ETAAC recommends the IRS take the following actions to meet its strategic challenges:

- Ensure all initiatives identified in *A Strategy for Growth* are incorporated within overall IRS strategic planning efforts. If the IRS cannot establish an overall strategic plan and planning process quickly, the IRS may not achieve its electronic tax administration goals.
- Apply the necessary resources to accomplish the initiatives described in *A Strategy for Growth* and create and implement an integrated strategic plan.
- Align electronic tax administration customer segments with the four business units now being established by the IRS organizational modernization plan.
- Develop a strategy to encourage every professional tax practitioner to file electronically. Professional tax practitioners include tax attorneys, Certified Public Accountants (CPAs), Enrolled Agents (EAs), and unlicensed tax preparers.
- Implement a strategic management process that is based on continual progress evaluation against established milestones, with provision for identifying new projects and corrective action. The ETAAC has assisted the IRS in identifying such a plan.
- Focus IT modernization on electronic transmission of information and engagement of the private sector for solutions rather than improvement of paper processes.
- Make electronic tax administration initiatives a high priority in the IRS IT modernization so they are synchronized with major IRS modernization blueprints rather than competing for attention in later years. It is imperative that IRS electronic tax administration projects be integrated into the IRS modernization blueprint at an early stage.
- Advertise taxpayer and preparer benefits for e-filing more aggressively. Effectively deliver and enhance such benefits to create taxpayer awareness and trust in e-filing.
- Continue to assign authentication, security, and privacy initiatives a high priority and continue to move forward quickly in this area. The 1999 tax filing season PIN and digital signature projects are major steps forward.
- Use *A Strategy for Growth* to articulate how partnerships with the private sector and governmental partners, such as states, can be facilitated and supported.

The ETACC recommends that Congress help the IRS achieve its electronic filing goals by maintaining high visibility on these goals in its oversight efforts, evaluating new legislative action where recommended by the IRS or ETAAC, and by appropriating the necessary funds for electronic tax administration and related technology infrastructure initiatives.

1.0 Introduction

Title II of the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 provided the IRS with the following policy statement with respect to electronic filing:

> It is the policy of Congress that
> (1) paperless filing should be the preferred and most convenient means of filing Federal tax and information returns
> (2) it should be the goal of the Internal Revenue Service to have at least 80 percent of all such returns filed electronically by the year 2007, and
> (3) the Internal Revenue Service should cooperate with and encourage the private sector by encouraging competition to increase electronic filing of such returns.

The full text of Title II of this legislation is contained in Appendix A.

Recognizing the importance of receiving private sector input to achieving this goal, the legislation further required that the IRS establish an electronic commerce advisory group to provide the IRS with private sector input, and further required that this advisory group report to Congress annually on the following subjects:

- the progress of the IRS in meeting the goal of receiving electronically 80 percent of tax and information returns by 2007
- the status of the strategic plan to eliminate barriers, provide incentives, and use competitive market forces to increase electronic filing gradually over the next ten years
- the legislative changes necessary to assist the IRS in meeting such goal
- the effects on small businesses and the self-employed of electronically filing tax and information returns

This report responds to the reporting requirements of the electronic commerce advisory group as specified in the IRS Restructuring and Reform Act of 1998, and can be valuable to Congress by providing independent assessments of:

- IRS plans from the private sector perspective
- Strategic challenges and opportunities facing the IRS
- Electronic filing impact on self-employed and small business
- Progress made by the IRS in achieving the goals established by Congress

2.0 The Role of the Electronic Tax Administration Advisory Committee

The Electronic Tax Administration Advisory Committee (ETAAC) satisfies the requirement of the IRS Restructuring and Reform Act to establish an electronic commerce advisory group. In this role, the ETAAC provides the IRS with advice from the private sector on how to achieve its electronic tax administration goals, with a primary focus on strategic issues and programs.

2.1 Charter

The charter for the ETAAC was developed by the IRS to meet the requirements of the legislation and was approved by the Department of Treasury. The current charter is contained in Appendix B.

2.2 ETAAC Member List and Organization

The members of the ETAAC were selected by the IRS to represent a broad spectrum of the private sector, including tax preparers, tax software developers, payroll companies, financial institutions, small businesses, state governments, and taxpayers. Appendix C contains the member list and its organizational structure.

2.3 Objectives for 1998-1999

The ETAAC's objectives for its first year of operation centered on understanding the strategic challenges facing the IRS, ensuring the IRS' strategic plan addressed these challenges as part of its strategic approach for achieving the goals established by Congress, and ensuring establishment of a process to evaluate progress and update future editions of the plan. The ETAAC identified the following specific objectives for 1998-1999:

- Assessing IRS' progress towards meeting its strategic electronic tax administration goals.
- Reviewing the IRS strategic plans relating to electronic tax administration.
- Identifying the strategic challenges facing the IRS.
- Assisting the IRS in developing a strategic planning process.

The first two objectives are statutorily required of the ETAAC by the IRS restructuring legislation, and the remainder address issues critical to achieving electronic tax administration goals by 2007. Results of the ETAAC's efforts to achieve these objectives are described in the next four sections of this report.

3.0 Assessing IRS Progress towards Meeting Strategic Goals

3.1 Filing Season Results

Electronic filing growth for 1999 is shown in Table 1. This year's increase of 19 percent is consistent with IRS projections and lends credence to the increases projected in *A Strategy for Growth* for subsequent years. However, the plan estimates a range of growth from 12 to 36 percent for the 2000 tax filing season. Based on this filing season's results, the ETAAC believes that unless new initiatives are implemented, such as the recommendations included in this report, the upper levels of the projections will not be achieved. The ETAAC believes that other strategies need to be implemented to ensure continual growth.

Table 1. Electronic Filing Growth for 1999

Electronic Returns	1999 Projected returns in millions (through 10/15/99)	1999 Actual returns in millions (through 6/18/99)	1998 Actual returns in millions	Percent Projected Change	Percent Actual Change
Practitioner	20.9	21.19	17.6	+1%	+20%
TeleFile	6.6	5.7	6.0	-14%	-5%
Online	2.1	2.4	.9	+14%	+161%
Totals	**29.6**	**29.2**	**24.6**	**-1%**	**+19%**

The cause of the decrease in TeleFile electronic returns is not yet known, although the decrease is consistent with overall Form 1040EZ filings, which were down 7.8 percent for paper and e-filed returns combined. Possible explanations include a shift to computer filings and the effect of new tax credits this year. The ETAAC recommends that the IRS analyze the causes of this decrease and factor them into future projections.

To put the growth achieved in 1999 in better perspective, Table 2 presents the growth of individual electronic tax returns for 1995 through 1999. The 19 percent growth achieved in 1999 is less than the growth achieved in each of the last three years. The ETAAC does not know if this slowing of the growth rate is a trend or an anomaly. The ETAAC recommends that the IRS monitor closely the total growth rate for electronic filing in future years.

Table 2. Five Year Growth of Electronic Filing for Individual Tax Returns

Year	Total Returns in millions	Practitioner Returns in millions	TeleFile Returns in millions	On-line Returns in millions	Total Electronic Returns in millions	Percent Change-Electronic Returns	Percent Change-Total Returns
1999	125.0	21.1	5.7	2.4	29.2	19%	2%
1998	122.5	17.6	5.9	0.9	24.4	26%	1%
1997	120.8	14.4	4.7	0.4	19.5	29%	2%
1996	118.8	12.1	2.8	0.2	15.1	28%	2%
1995	116.5	11.1	0.7	0.001‘	11.8	N/A	N/A

Results for new payment initiatives are shown in Table 3.

Table 3. Payment Initiatives Results.

Payment Initiatives	1999 Projected	1999 Actual
Credit card payments		53,063
ACH payments		74,339
Total electronic payments	**300,000**	**127,402**

In other results, the IRS issued Electronic Customer Numbers (ECNs) for the Online Filing PIN Pilot to 1 million online and 7 million paper filers. Because of joint return situations, a total of 12 million ECNs were issued. Of these filers, 649,576 used the PINs, a participation rate of 8 percent. The IRS also enrolled 8,100 Electronic Return Originators (EROs) in the Practitioner PIN Pilot. Of these practitioners, 2,493 participated in this pilot for a total of 496,119 returns.

All employers with gross federal tax receipts in excess of $200,000 are to use the Electronic Federal Tax Payment System (EFTPS). As of March 20, 1999, 94 percent of the mandated employers were enrolled, with 91 percent actually using EFTPS. Also, 48 percent of non-mandated employers are also using EFTPS for tax deposits. Volunteer enrollments increased by 264,547, although the percentage of users actually went down by about 8 percent. The new enrollments are due to trust enrollments, which may increase EFTPS use, as this new class of users becomes familiar with its operation.

3.2 Accomplishments During 1998-1999

In addition to the overall 19 percent growth in e-filed returns, the 1999 tax filing season included several noteworthy events that reflect positively on the abilities of the IRS to successfully administer a growing electronic tax administration program.

Publication of ETA Strategic Plan
The publication of the IRS document, *A Strategy for Growth* is a notable IRS achievement. Publication of this document in December 1998 was a key milestone in defining IRS vision, mission, and strategies for electronic tax administration expansion. The publication of the document set a positive direction for implementation of plans specific to the 1999 tax filing season.

Business Continuity
During the early part of the 1999 tax filing season, some electronic return transmitters experienced problems in transmitting to the Andover, Austin and Cincinnati Service Centers. In the case of Cincinnati, telecommunications and hardware problems quickly were diagnosed and solved to minimize disruption to transmitters and to avoid the loss of return data. In addition, returns transmitted to Cincinnati via some telecommunications networks were shifted to the IRS Tennessee Computing Center's Electronic Management System to better handle increasing volumes. In the cases of the Andover and Austin Service Centers, problems in processing returns with Electronic Customer Numbers caused delays in processing electronic returns.

Although these problems caused some initial confusion for transmitters and EROs, the IRS reacted quickly by notifying affected parties, repairing hardware, and re-routing and shifting transmissions. Nevertheless, the Andover system had to be shut down over a weekend to re-load files that had been archived several weeks earlier and, therefore, were not available as needed during a busy period. After all the 1999 tax filing season problems were resolved, transmission patterns and electronic processing returned to normal. It is noteworthy that the IRS plans to modify procedures and policies to avoid a repeat of these incidents in the 2000 tax filing season.

Increased use of electronic tax administration couples stakeholders more tightly with IRS systems compared to paper operations. For example, unexpected problems such as those discussed above have a ripple effect on electronic filers. During peak week, even one-day delays create bottlenecks that are difficult to manage. The ETAAC recommends that IRS plans for operational readiness and disaster recovery include notification to tax preparers, states, and taxpayers if problems occur. The newly approved ETA Account Management program could have an important role in the notification process. This same program might also help to address urgent e-filing problems large transmitters face during the filing season. More importantly, however, the IRS should implement systems with excess capacity and full redundancy, ensuring 100% availability.

ERO Growth

During the practitioner-focused e-filing promotional campaign conducted prior to the 1999 tax filing season, the IRS aggressively invited thousands of tax practitioners to become active EROs. *A Strategy for Growth* envisions 100,000 paid preparer EROs e-filing individual and business tax returns. At the present time, 89,881 professional preparers are enrolled; however, only 61,811 EROs filed at least one tax return to maintain their professional status as EROs. Further analysis of IRS 1999 data indicates that 55 percent of these active EROs e-file over 95 percent of all e-filed returns. The ETAAC recommends that IRS continue its research efforts to identify the factors that will motivate tax professionals to be active participants in e-filing.

ETA Account Management Organizational Initiative

Recognizing that the existing marketing and promotion programs for e-filing need to be improved and expanded, the IRS ETA group proposed a new account management organization that has the potential to significantly accelerate practitioner, industry and state agency participation in various promotional programs. The IRS has made a decision to implement account management in time to see results as early as the 2000 tax filing season.

Volunteer, Military and Walk-in Site Participation

During the 1999 tax filing season, nearly 900,000 electronic returns were transmitted from sites that offered e-filing to the military, “walk-in” customers at IRS offices, IRS employees, AARP clients and other nonmilitary visitors to Volunteer Income Tax Assistance sites. The e-filing growth of in 1999 suggests that IRS outreach efforts to these segments was a success, and suggests that further efforts to support e-filing from these sources is a worthwhile component of the overall IRS marketing, advertising and outreach plans.

3.3 Progress Towards Meeting Strategic Goals

The IRS Restructuring and Reform Act of 1998 established a goal for the IRS that 80 percent of all tax and information returns should be filed electronically by the year 2007. The act further requires that the IRS strategic plan for reaching the 80 percent goal provide that all such returns **prepared** electronically should be **filed** electronically by the 2003 tax filing season.

The 2003 goal aims to reach 100 percent electronic filing of all returns prepared on computer by both tax professionals and taxpayers alike. While progress is being made, the ETAAC believes that much work remains to be done to even approach this goal. Many new initiatives are needed on both fronts—attracting more professional tax preparers to register with the IRS as EROs and altering their systems in favor of electronic filing, and to attract more electronic filing from taxpayers who prepare their own returns on computers. The IRS needs to focus on a segmented approach that provides differing incentives for these very diverse groups of filers. The ETAAC has reviewed strategic initiatives in place for the 2000 tax filing season and has been briefed on many of the initiatives in process for subsequent years. The ETAAC believes that the goal for

2003 is not achievable without considering a broader set of initiatives or incentives than is currently planned, including consideration of incentives that require legislative action.

The ETAAC believes that setting a goal of having all electronically prepared returns filed electronically is an excellent strategy. This goal is an important achievement, even if it cannot be achieved by 2003. However, failure to achieve the 2003 goal will also put the 2007 goal of 80 percent electronic filing of all returns in jeopardy. The question should not be whether the IRS will meet its 2007 goal, but rather, what types of initiatives and incentives are required to change taxpayer and tax preparer behavior so this goal can be achieved. The ETAAC believes that more new initiatives and incentives will be needed to achieve the 2007 goal. Moreover, it is critical that the IRS develop new initiatives quickly and have a program to evaluate results against established milestones and expectations.

The two-year request and approval process for Request for Information Services (RIS) and for budgetary resources must be considered in planning to achieve the 80 percent goal by 2007. In fact, 2007 is two years closer than it appears as all final plans and resources will be initiated and requested no later than 2005. Hence, from a budget and planning perspective, we are only five years away from the final goal. The IRS must carefully and critically select projects, define information system changes, and budget in each of the five remaining years.

4.0 Reviewing the ETA Strategic Plan.

A major activity performed by the ETAAC during this reporting period was to review the first Internal Revenue Service (IRS) electronic tax administration strategic plan, *A Strategy for Growth*, issued in December 1998. The development of *A Strategy for Growth* is a notable achievement. IRS must build on this good start by sustained effort to mature the strategic plan. However, a strategy that will achieve the goal of having at least 80 percent of all Federal tax and information returns filed electronically by the year 2007 is not yet complete. *A Strategy for Growth* projects 49.4 to 70.4 million form 1040 e-filed returns in the year 2007, which is substantially short of the 80 percent goal.

The ETAAC made a thorough review of *A Strategy for Growth*. The ETAAC's recommendations are included in Appendix D. A summary of recommended actions that the ETAAC believes the IRS must take to achieve the electronic filing goals established by Congress include:

- Monitor the IRS strategic plan to ensure it integrates and supports *A Strategy for Growth*, particularly in the information technology (IT) area.
- Document a process for identifying new projects, refining and assessing annual performance measures, and updating the strategic plan to move toward achievement of the goals.
- Align electronic tax administration customer segments with the four business units now being established by the IRS organizational modernization plan.
- Focus IT modernization on electronic transmission of information and engagement of the private sector for solutions rather than improvement of paper processes.

- Make electronic tax administration initiatives a high priority in the IRS IT modernization so they are synchronized with major IRS modernization blueprints rather than competing for attention in later years. It is imperative that IRS ETA projects be integrated into the IRS modernization blueprint at an early stage.
- Advertise taxpayer and preparer benefits for e-filing more aggressively. Effectively deliver and enhance such benefits to create taxpayer awareness and trust in e-filing.
- Continue to assign authentication, security, and privacy initiatives a high priority and continue to move forward quickly in this area. The 1999 tax filing season PIN and digital signature projects are major steps forward.
- Give electronic tax administration development projects adequate resources and authority for pilots and prototypes, enabling quick responses to the rapid change in the electronic commerce marketplace.
- Monitor ERO concerns to ensure that EROs perceive and receive benefits and incentives that are greater than paper preparers. Handle suspensions in a timely, effective and fair manner that is geared toward keeping EROs in the system rather than excluding them, except in cases of abuse.
- Use *A Strategy for Growth* to articulate how partnerships with the private sector and other government partners such as states can be facilitated and supported. As the plan matures and additional initiatives are added, continue to identify to the private sector those projects the IRS intends to develop internally and which projects will be "released" to the private sector so that duplicate resources are not wasted by private partners on IRS internal projects.

5.0 Strategic Challenges and Opportunities

The ETAAC believes that the IRS faces a number of strategic challenges and opportunities while seeking to achieve the primary e-filing goals of having all returns prepared electronically to be filed electronically by 2003 and getting 80 percent of all returns filed electronically by 2007.

5.1 Strategic Challenges

The ETAAC believes that the IRS faces business, internal management, and technology challenges in achieving its electronic tax administration goals.

Business challenges
The ETAAC believes that the IRS must make electronic tax administration the usual method of interacting with the IRS by:

- Creating new processes and incentives for electronic tax administration that deliver value to all taxpayer segments (individuals, small businesses, large corporations, and tax-exempt organizations).
- Developing a strategy that provides strong incentives to all professional tax practitioners to enroll as EROs.
- Convincing taxpayers and professional tax preparers, through communications and marketing, that e-filing should be the filing method of choice.

Internal Management Challenges

The ETAAC believes that the IRS must make electronic tax administration a priority for all its organizational elements by:

- Transitioning to a customer-centric organization providing taxpayers with customer-segmented, tailored, and responsive products and services while concurrently transitioning to electronic services and systems and maintaining legacy systems that support paper filing.
- Integrating agency-wide strategic plans, including *A Strategy for Growth*, the Modernization Blueprint, and the organizational modernization plan into one cohesive business and strategic plan for the Service.
- Ensuring adequate resources are committed to the implementation of electronic tax administration projects and initiatives.
- Holding the executives of each new operating division accountable for achieving the electronic tax administration goals for the taxpayer segment assigned to the division.

Technology Challenges

The ETAAC believes that the IRS must support electronic tax administration goals with technology by:

- Implementing the necessary technology infrastructure to support the IRS electronic tax administration business goals, including security, authentication, privacy, database, and communications systems.
- Developing and maintaining the ability to receive electronically all the forms from all types of returns from all filers.
- Developing a scalable technology architecture that will support the growing volumes associated with achieving the electronic tax administration business goals.

The ETAAC is pleased with IRS plans to accelerate the development of the technology infrastructure needed for electronic filing, particularly IRS' consideration of re-writing the IRS Master File as soon as possible and populating it with e-file data. This project would provide the platform for improved IRS customer support for those who e-file, and additional services to support and encourage professional preparers to e-file returns.

Development and implementation of new technical infrastructure is critical to reaching electronic tax administration goals. Implementing this technical infrastructure requires funding from the Information Technology Investment Account established by Congress in FY 1998. Funds in this account cannot be spent until approved by Congress. While the ETAAC recognizes that there are many issues surrounding Congressional release of these funds, it urges Congress to give timely consideration to IRS' request for these funds, and approve their use as soon as the IRS satisfies the necessary conditions.

5.2 Strategic Opportunities

Although facing a number of strategic challenges, the IRS also has many opportunities to use electronic tax administration to change the way taxpayers and other stakeholders interact with the agency. Examples of these opportunities are discussed below.

A growing number of Americans can access the Internet and do so regularly. According to a recent Department of Commerce report, about 80 million Americans are online, and 42.2 percent of the U.S. adult population are regular Internet users. *A Strategy for Growth* indicates that the IRS must position itself to take full advantage of the public's growing acceptance and use of the Internet. The ETAAC strongly endorses the formulation of an Internet strategy. Current initiatives such as e-mail based customer service, web-enabled delivery of content for inquiry purposes via the IRS home page, and internal consolidation of 11 e-mail systems to one system all provide a solid foundation for an Internet strategy. As new security and privacy safeguards are developed, the ETAAC recommends that the IRS fully leverage these opportunities and provide value bearing, account related transactions over the Internet.

The ETAAC believes the IRS has opportunities to expand its business partnerships with the following stakeholder groups that support its electronic tax administration goals:

- Professional preparers
- Large transmitters and software providers
- Payroll and tax processors
- State taxing agencies

Professional preparers
The ETAAC believes that full participation in electronic filing by nearly all tax preparers is a necessity if the IRS is to achieve the 80 percent goal. The IRS must seize the opportunity to encourage tax preparers to enroll as EROs and make the ERO program attractive to tax preparers. The ERO program should be designed to assist preparers achieve their business goals, including minimization of costs, maximization of productivity, convenience, technology and professional peer acceptance. Practitioners need a single filing methodology that can easily be incorporated into their processing routines. Incentives such as receipt of client acknowledgments, on-line access to client return information once an electronic Power of Attorney (POA) has been filed, and error checking of Taxpayer Identification Numbers (TINs) would be welcomed by the practitioner community and would increase ERO participation.

One area of concern to the preparer community is the disparity between standards for paper return preparers as compared to the standards for EROs. The ETAAC understands that the IRS is investigating this inequity and encourages the IRS to consider additional regulations for professional tax preparers that would treat all tax preparers equally, regardless of the method of filing. The IRS should not send a message to paper filers, however unintentional, that filing only by paper results in the absence of standards.

While the ETAAC endorses the need for standards for EROs, it does recommend a review of suspension regulations. In this regard, IRS should re-evaluate whether current suspension penalties are appropriate for the offense and whether appropriate due process safeguards and rights of appeal are in place.

Another area not to be overlooked is the vast network of volunteer organizations that provide much-needed tax assistance for elderly and low-income taxpayers. Giving qualified volunteer organizations the ability to e-file would provide an excellent opportunity for citizens in rural and inner-city areas to receive the same quality electronic services that are provided by commercial preparers.

Software developers and third party transmitters
Software developers and third party transmitters that develop business applications are potential providers of data to the IRS. This group includes developers of corporate, payroll, and financial reporting software programs. The ETAAC believes that developing partnerships with these organizations provides another excellent opportunity to further the IRS e-file goals.

Payroll and Tax Processors
Payroll and Tax Filing service providers are pleased their industry was mentioned in the IRS' plans relating to the National Accounts Program. Additionally, the industry was pleased to see the diversity of products and services the IRS plans for payroll related tax filings such as EDI-enabled processes, proprietary trading partner interfaces, and Internet filing options.

The ETAAC believes that appropriate incentives should be made available to these practitioners in order to increase electronic filings and reduce tax reporting burdens. For example, once a Reporting Agent Authorization (RAA) has been filed, payroll and tax filing service providers should be provided with regular electronic notice of tax deposit schedules and Employer Identification Numbers (EINs), as well as on-line access to client return information and electronic delivery of IRS notices.

State taxing agencies
The state taxing agencies are interested in the continued and improved revenue protection strategies, while increasing the use of their electronic options. Because many states are technologically advanced in their tax collection activities, the IRS should take the opportunity to involve them heavily in the e-file and modernization efforts. Partnership with state tax agencies can truly be a mutually beneficial partnership for both the IRS and the states.

Federal-state planning and cooperation provides the opportunity to reduce the filing and payment transaction burden not only for individuals, but for business and corporate taxpayers. As the IRS expands electronic filing and payment programs for businesses, partnerships and corporations, the ETAAC recommends that the IRS continue to investigate improved methods of partnering with states.

In addition to the business partnerships with third party stakeholders noted above, the ETAAC believes that the IRS has an opportunity to expand its relationships with the taxpaying public and businesses as described below.

Taxpaying public
Convincing individuals who prepare their returns manually to switch to an electronic method will require a major change in public attitudes. The IRS has an obligation, as well as a great opportunity, to continue and expand its public awareness of how and why the e-file programs offer taxpayers safety, accuracy, convenience, and additional future services. The ETAAC believes that the IRS should continue its research on identifying the factors that will motivate individual taxpayers to make electronic filing the preferred method. Understanding taxpayer behavior to the greatest possible depth is critical to developing the most effective incentives.

Business
The ETAAC encourages IRS to use a Business-to-Business Model, conducting business electronically with business taxpayers in a similar fashion that businesses already conduct business electronically with each other. The ongoing IRS organizational modernization plan has separate business units and should foster this type of model. The following examples illustrate the benefits of such a model:

Business Partnering—When a business partnership is entered into, it is done so to provide benefits for both parties. The IRS is encouraged to find innovative ways to achieve mutually beneficial relationships with its stakeholders.

Use common practices—the ETAAC recommends that the IRS consider using technologies and practices that are common within the business world. In the long run this will help keep programs up to date and reduce the cost of maintaining programs that may be unique to the IRS. The ETAAC also encourages common business practices with related federal agencies, such as Social Security Administration (SSA). Because these two agencies are not sharing similar business practices, the ETAAC believes this leads to frustration and confusion of the taxpayer.

Multiple Customer Segments—the ETAAC believes that the IRS must support electronic tax administration by creating a business model that recognizes that it has multiple customer segments, and be willing and able to meet the needs of those multiple customers, such as:

- By understanding the business decision process of each customer segment, the IRS will be able to derive the optimum strategic or technical solution for different customer segments such as large and small businesses.
- By understanding that the distribution channels available contain customers with different set of business decision values, the IRS will be able to accomplish its goals. The IRS must ensure that it is not competing with its distribution channel, otherwise the benefits gained will not be fully achieved.

The IRS decision to organize around customer segments will be helpful in developing effective approaches. The ETAAC believes that the IRS must segment its electronic tax administration business processes to achieve a “best practices” approach. For example, one segment could consist of bulk filers, or consolidators, so that the needs of the third party filer distribution channel can best be met. Ensuring the needs of this segment is critical to meet the needs of mass volume producers. Tax preparers could comprise a second segment since a different set of ethics rules might apply. A third segment, which could be further segmented into small and large businesses, could be businesses that self file their returns. The ETAAC believes that the IRS should continue its research on identifying the factors that will motivate business taxpayers to make electronic filing the preferred method. Understanding taxpayer behavior to the greatest possible depth is critical to developing the most effective incentives.

An analysis of the effects of electronic filing on all size businesses is found in Appendix E.

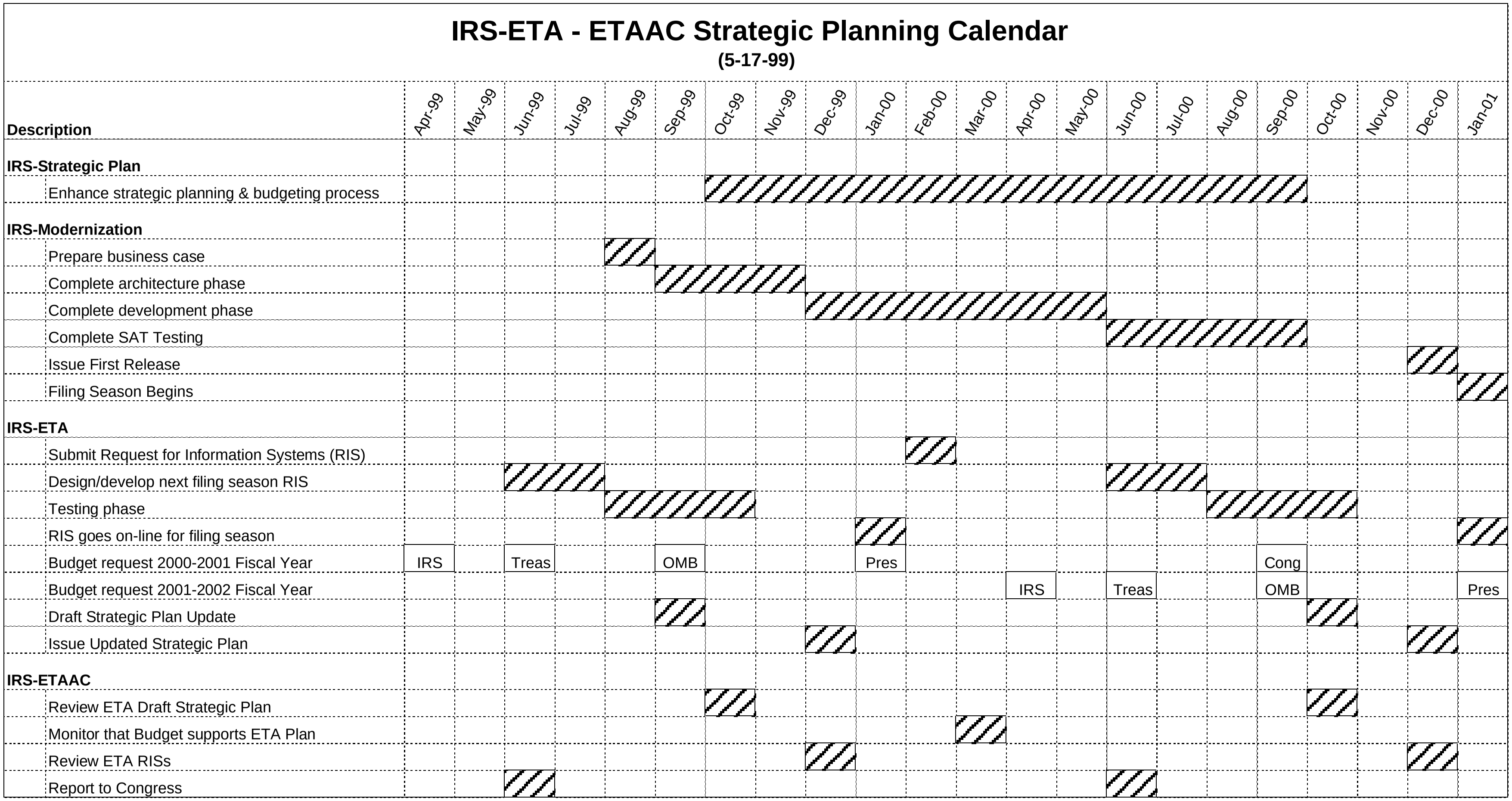
6.0 Assisting IRS Define a Strategic Planning Process

The IRS is at a seminal stage in development of an overall strategic planning process and is in the throes of reorganizing the agency into four business units. The IRS ETA (electronic tax administration) group is ahead of the agency as a whole in development of a strategic planning process. The ETAAC believes that the IRS must progress significantly in the integration of electronic tax administration objectives into an overall IRS strategic plan. If the IRS cannot establish an overall strategic plan and planning process quickly, the IRS may not achieve its electronic tax administration goals; particularly obtaining 80 percent of all tax returns electronically filed by 2007.

IRS issued its first electronic tax administration strategic plan, *A Strategy for Growth*, in December 1998, and will issue a second revised plan in December 1999. The IRS-ETA group has worked cooperatively with the ETAAC to develop a mutually agreed-to Strategic Planning Calendar, shown in Table 4, as a common baseline from which more detailed planning methods and measurements will be taken. The ETA group intends to articulate additional detail on how it will operationalize the strategic planning process to accomplish individual initiatives in its December 1999 revised strategic plan.

The ETAAC believes that the ETA organization has taken a solid step forward in strategic planning, but much remains to be accomplished, particularly by the IRS in its overall strategic planning process. The ETAAC recommends that the ETA group re-estimate its goals and intermediate milestones based on knowledge acquired since the release of the original ETA strategic plan and henceforth continue this process on an annual basis. The ETAAC further suggests the initiatives developed by ETA contain quantitative measures reflecting the expected return on effort for each initiative. These analyses should include costs and benefits expected for the IRS, the customer, other affected parties, and should be shared with the ETAAC in advance, allowing the ETAAC the opportunity to assess and evaluate the intended direction and advise the IRS prior to program approval and implementation. Additionally, the ETAAC recommends that the IRS-ETA group report on the status of the business goals enumerated in Appendix C of *A Strategy for Growth* on an annual basis.

Table 4. IRS ETA Strategic Planning Calendar



7.0 Conclusions

The ETAAC concludes that the IRS, by establishing a separate group to focus on electronic tax administration matters, has helped provide executive attention to the achievement of its electronic tax administration goals. The overall goal will only be achieved by placing responsibility for achieving electronic tax administration goals with each business unit in addition to the ETA group. IRS must integrate its agency-wide strategic plans, *A Strategy for Growth*, the Modernization Blueprint, and the organizational modernization plan into one cohesive business and strategic plan for the Service, and make improved electronic tax administration a vital part of the way IRS does business with taxpayers in the future. All other actions flow from establishing this strategic focus on electronic tax administration.

The ETAAC believes it is critical that the IRS have a comprehensive program to evaluate progress against established milestones and expectations, with provision for identifying new initiatives and incentives as necessary. A fundamental question for both Congress and the IRS is what initiatives and incentives will be required to meet the electronic filing goals for 2007. The ETAAC believes that a broader set of initiatives or incentives than is currently planned will be necessary to achieve this goal. The broadest range of initiatives and incentives should be considered, including those that require legislative action, and Congress must be ready to enact incentives legislatively if the IRS can demonstrate that such action is necessary. While this report does not identify any specific recommendations that require legislative action, future reports from the ETAAC may recommend such action.

The ETACC recommends that Congress help the IRS achieve its electronic filing goals by maintaining high visibility on these goals in its oversight efforts, evaluating new legislative action where recommended by the IRS or ETAAC, and by appropriating the necessary funds for electronic tax administration and related technology infrastructure initiatives.

If the IRS can provide improved services that influence taxpayer behavior so that most taxpayers choose to interact with the IRS electronically, it will have made a major step towards delivering the type of improved customer service envisioned by the National Commission on Restructuring the IRS and intended by the IRS Restructuring and Reform Act of 1998.

Appendix A
IRS Restructuring and Reform Act of 1998

TITLE II—ELECTRONIC FILING

SEC. 2001. ELECTRONIC FILING OF TAX AND INFORMATION RETURNS.

(a) IN GENERAL.— It is the policy of Congress that—

(1) paperless filing should be the preferred and most convenient means of filing Federal tax and information returns;

(2) it should be the goal of the Internal Revenue Service to have at least 80 percent of all such returns filed electronically by the year 2007; and

(3) the Internal Revenue Service should cooperate with and encourage the private sector by encouraging competition to increase electronic filing of such returns.

(b) STRATEGIC PLAN.—

(1) IN GENERAL.— Not later than 180 days after the date of the enactment of this Act, the Secretary of the Treasury or the Secretary's delegate (hereafter in this section referred to as the "Secretary") shall establish a plan to eliminate barriers, provide incentives, and use competitive market forces to increase electronic filing gradually over the next 10 years while maintaining processing times for paper returns at 40 days. To the extent practicable, such plan shall provide that all returns prepared electronically for taxable years beginning after 2001 shall be filed electronically.

(2) ELECTRONIC COMMERCE ADVISORY GROUP.— To ensure that the Secretary receives input from the private sector in the development and implementation of the plan required by paragraph (1), the Secretary shall convene an electronic commerce advisory group to include representatives from the small business community and from the tax practitioner, preparer, and computerized tax processor communities and other representatives from the electronic filing industry.

(c) PROMOTION OF ELECTRONIC FILING AND INCENTIVES.— Section 6011 is amended by redesignating subsection (f) as sub-section (g) and by inserting after subsection (e) the following new subsection:

"(f) PROMOTION OF ELECTRONIC FILING.—

"(1) IN GENERAL.— The Secretary is authorized to promote the benefits of and encourage the use of electronic tax administration programs, as they become available, through the use of mass communications and other means.

"(2) INCENTIVES.— The Secretary may implement procedures to provide for the payment of appropriate incentives for electronically filed returns.”.

(d) ANNUAL REPORTS.— Not later than June 30 of each calendar year after 1998, the Chairperson of the Internal Revenue Service Oversight Board, the Secretary of the Treasury, and the Chair-person of the electronic commerce advisory group established under subsection (b)(2) shall report to the Committees on Ways and Means, Appropriations, Government Reform and Oversight, and Small Business of the House of Representatives and the Committees on Finance, Appropriations, Governmental Affairs, and Small Business of the Senate on—

(1) the progress of the Internal Revenue Service in meeting the goal of receiving electronically 80 percent of tax and information returns by 2007;

(2) the status of the plan required by subsection (b);

(3) the legislative changes necessary to assist the Internal Revenue Service in meeting such goal; and

(4) the effects on small businesses and the self-employed of electronically filing tax and information returns.

SEC. 2002. DUE DATE FOR CERTAIN INFORMATION RETURNS.

(a) INFORMATION RETURNS FILED ELECTRONICALLY.— Section 6071 (relating to time for filing returns and other documents) is amended by redesignating subsection (b) as subsection (c) and by inserting after subsection (a) the following new subsection:

“(b) ELECTRONICALLY FILED INFORMATION RETURNS.— Returns made under subparts B and C of part III of this subchapter which are filed electronically shall be filed on or before March 31 of the year following the calendar year to which such returns relate.”.

(b) STUDY RELATING TO TIME FOR PROVIDING NOTICE TO RECIPIENTS.—

(1) IN GENERAL.— The Secretary of the Treasury shall conduct a study evaluating the effect of extending the deadline for providing statements to persons with respect to whom information is required to be furnished under subparts B and C of part III of subchapter A of chapter 61 of the Internal Revenue Code of 1986 (other than section 6051 of such Code) from January 31 to February 15 of the year in which the return to which the statement relates is required to be filed.

(2) REPORT.— Not later than June 30, 1999, the Secretary of the Treasury shall submit a report on the study under paragraph (1) to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate.

(c) EFFECTIVE DATE.— The amendment made by subsection (a) shall apply to returns required to be filed after December 31, 1999.

SEC. 2003. PAPERLESS ELECTRONIC FILING.

(a) IN GENERAL.— Section 6061 (relating to signing of returns and other documents) is amended—

(1) by striking “Except as otherwise provided by” and inserting the following:

“(a) GENERAL RULE.— Except as otherwise provided by sub-section (b) and”; and

(2) by adding at the end the following new subsection:

“(b) ELECTRONIC SIGNATURES.—

“(1) IN GENERAL.— The Secretary shall develop procedures for the acceptance of signatures in digital or other electronic form. Until such time as such procedures are in place, the Secretary may—

“(A) waive the requirement of a signature for; or

“(B) provide for alternative methods of signing or subscribing,

a particular type or class of return, declaration, statement, or other document required or permitted to be made or written under internal revenue laws and regulations.

“(2) TREATMENT OF ALTERNATIVE METHODS.— Notwithstanding any other provision of law, any return, declaration, statement, or other document filed and verified, signed, or subscribed under any method adopted under paragraph (1)(B) shall be treated for all purposes (both civil and criminal, including penalties for perjury) in the same manner as though signed or subscribed.

“(3) PUBLISHED GUIDANCE.— The Secretary shall publish guidance as appropriate to define and implement any waiver of the signature requirements or any method adopted under paragraph (1).”.

(b) ACKNOWLEDGMENT OF ELECTRONIC FILING.— Section 7502(c) is amended to read as follows:

“(c) REGISTERED AND CERTIFIED MAILING; ELECTRONIC FILING.—

“(1) REGISTERED MAIL.— For purposes of this section, if any return, claim, statement, or other document, or payment, is sent by United States registered mail—

“(A) such registration shall be prima facie evidence that the return, claim, statement, or other document was delivered to the agency, officer, or office to which addressed; and

“(B) the date of registration shall be deemed the post-mark date.

“(2) CERTIFIED MAIL; ELECTRONIC FILING.— The Secretary is authorized to provide by regulations the extent to which the provisions of paragraph (1) with respect to prima facie evidence of delivery and the postmark date shall apply to certified mail and electronic filing.”.

(c) ESTABLISHMENT OF PROCEDURES FOR OTHER INFORMATION.— In the case of taxable periods beginning after December 31, 1999, the Secretary of the Treasury or the Secretary’s delegate shall, to the extent practicable, establish procedures to accept, in electronic form, any other information, statements, elections, or schedules, from taxpayers filing returns electronically, so that such taxpayers will not be required to file any paper.

(d) INTERNET AVAILABILITY.— In the case of taxable periods beginning after December 31, 1998, the Secretary of the Treasury or the Secretary’s delegate shall establish procedures for all tax forms, instructions, and publications created in the most recent 5-year period to be made available electronically on the Internet in a searchable database at approximately the same time such records are available to the public in paper form. In addition, in the case of taxable periods beginning after December 31, 1998, the Secretary of the Treasury or the Secretary’s delegate shall, to the extent practicable, establish procedures for other taxpayer guidance to be made available electronically on the Internet in a searchable database at approximately the same time such guidance is available to the public in paper form.

(e) PROCEDURES FOR AUTHORIZING DISCLOSURE ELECTRONICALLY.— The Secretary shall establish procedures for any taxpayer to authorize, on an electronically filed return, the Secretary to disclose information under section 6103(c) of the Internal Revenue Code of 1986 to the preparer of the return.

(f) EFFECTIVE DATE.— The amendments made by this section shall take effect on the date of the enactment of this Act.

SEC. 2004. RETURN-FREE TAX SYSTEM.

(a) IN GENERAL.— The Secretary of the Treasury or the Secretary’s delegate shall develop procedures for the implementation of a return-free tax system under which appropriate individuals would be permitted to comply with the Internal Revenue Code of 1986 without making the return required under section 6012 of such Code for taxable years beginning after 2007.

(b) REPORT.— Not later than June 30 of each calendar year after 1999, the Secretary shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on—

(1) what additional resources the Internal Revenue Service would need to implement such a system;

(2) the changes to the Internal Revenue Code of 1986 that could enhance the use of such a system;

(3) the procedures developed pursuant to subsection (a); and

(4) the number and classes of taxpayers that would be permitted to use the procedures developed pursuant to sub-section (a).

SEC. 2005. ACCESS TO ACCOUNT INFORMATION.

(a) IN GENERAL.— Not later than December 31, 2006, the Secretary of the Treasury or the Secretary's delegate shall develop procedures under which a taxpayer filing returns electronically (and their designees under section 6103(c) of the Internal Revenue Code of 1986) would be able to review the taxpayer's account electronically, but only if all necessary safeguards to ensure the privacy of such account information are in place.

(b) REPORT.— Not later than December 31, 2003, the Secretary of the Treasury shall report on the progress the Secretary is making on the development of procedures under subsection (a) to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate.

Appendix B

AMENDED CHARTER FOR THE ELECTRONIC TAX ADMINISTRATION ADVISORY COMMITTEE (ETAAC) OF THE INTERNAL REVENUE SERVICE

This charter is prepared and filed in accordance with the provisions of the Federal Advisory Committee Act, Public Law 92-463, enacted October 6, 1972. ***It was required by the IRS Restructuring and Reform Act of 1998, Title II, Section 2001(b)(2).***

Official Title. The group's official title is the Electronic Tax Administration Advisory Committee (ETAAC).

Objectives and Scope. The ETAAC is being established to provide continued input into the development and implementation of the Internal Revenue Service' (IRS') strategy for electronic tax administration. The ETAAC will provide an organized public forum for discussion of electronic tax administration issues in support of the overriding goal that paperless filing should be the preferred and most convenient method of filing tax and information returns. The ETAAC members will convey the public's perceptions of IRS electronic tax administration activities, offer constructive observations about current or proposed policies, programs, and procedures, and suggest improvements.

The ETAAC is authorized to advise the Department of Treasury and the Internal Revenue Service on electronic tax administration issues. The Assistant Commissioner (Electronic Tax Administration) will assure that the size and organizational representation of the ETAAC obtains balanced membership and includes representatives from the tax practitioner, preparer, and computerized tax processor communities, the small business community and other representatives from the electronic filing industry. Nominations will be solicited from professional and public interest groups, IRS officials, the Department of Treasury, and Congress. Members will be limited to serving one two-year term on the ETAAC to ensure that new perspectives and ideas are generated by the members.

This activity is based on the authority to administer the Internal Revenue laws conferred upon the Secretary of the Treasury by section 7802 of the Internal Revenue Code and delegated to the Commissioner of the Internal Revenue.

Time Period. The period of time necessary for the ETAAC to carry out its duties is indeterminate since there will be a continuing need for the Department of Treasury and the IRS to receive suggestions and constructive criticism regarding its strategy for electronic tax administration. No termination date of less than two years from the date of this charter has been established.

D. Reporting. The ETAAC reports to the Assistant Commissioner (Electronic Tax Administration).

1. Support Services. The IRS provides the necessary support services for the ETAAC.

2. Duties. The ETAAC's duties are to research, analyze, consider, and make recommendations on a wide range of electronic tax administration issues and to provide input into the development and implementation of the strategic plan for electronic tax administration. The Chairperson of the ETAAC, in conjunction with the Chairperson of the Internal Revenue Service Oversight Board and the Secretary, shall report annually to the Congress on (1) the progress of the IRS in meeting the goal of receiving electronically 80 percent of tax and information returns by 2007; (2) the status of the strategic plan for electronic tax administration; (3) the legislative changes necessary to assist the IRS in meeting such goal; ***and (4) the effects on small businesses and the self-employed of electronically filing tax and information returns.***

3. Annual Operating Costs. The estimated annual operating costs are $75,000 and one staff year. Annual operating costs include travel, staff salary, and representation fund operating expenses. Committee members are not paid for their time or services. Members will be reimbursed for their travel related expenses to attend public meetings, ***working sessions***, and one orientation session per year, in accordance with 5 U.S.C. §5703 (as for persons employed intermittently in the Government service). Except as expressly stated above, the Government shall not be responsible for any expenses incurred by or on behalf of ETAAC members as a result of their application to, membership in, and activities for the ETAAC.

4. Number and Frequency of Meetings. The ETAAC generally meets four times a year: two public meetings and two working sessions. In addition, an orientation session is held each year.

1. Termination Date. No termination date has been determined. The charter will be submitted for renewal two years from the filing date listed in item "J.".

1. Filing Date. The date of filing of the original charter was March 27, 1998. The date of filing of this amended charter is ____________________.

Submitted by:

/s/ 12/18/98

Charles O. Rossotti
Commissioner of Internal Revenue Service

Date

Approved by:

/s/ 1/27/98

Nancy Killefer
Assistant Secretary for Management and CFO

Date

Appendix C
ETAAC Member List and Organizational Structure

The ETAAC has organized itself into three subgroups to carry out its role:

- Strategic Planning Subgroup
- Individual Taxpayer Subgroup
- Business Taxpayer Subgroup

The ETAAC assigned each subgroup the following responsibilities:.

The Strategic Planning Subgroup's responsibilities include:

- Review the IRS strategic plan and planning process
- Assess whether the plan can achieve ETA goals
- Confirm ETA and IRS strategic plans align

The Individual Subgroup's responsibilities include:

- Identify potential private/public sector partnerships
- Review IRS plans for proposed ETA projects and assess results
- Assist to resolve disputes between IRS and private sector

The Business Subgroup's responsibilities include:

- Identify potential private/public sector partnerships
- Review IRS plans for proposed ETA projects and assess results
- Identify the effects on small businesses and the self-employed of electronically filing tax and information returns

The ETAAC membership list and organizational assignments are shown below.

Chair: Charles A. Lacijan, Sr. Technical Advisor, The Implementation Group

Strategic Planning Working Group

William C. Shepard (Chair), VP & General Manager, Professional Products Group, Intuit, Inc.
Michael P. Boyle, Chief Tax Counsel & General Auditor, Microsoft Corp.
Robert O. Lewis, President, Tax Back, Inc.
Susan W. Martin, Professor of Accounting & Taxation, Grand Valley State University
Bette Rice, Director, Enterprise Technology Services, Merrill Lynch

Individual Working Group

Connie L. Grimes (Chair), President, Grimes Income Tax, Inc.
Margaret Drescher, National Advisor, Chair National Technology Committee, AARP

Edward B. Feinstein, AVP, Electronic Commerce, H&R Block Tax Services
Mary B. Harris, Jackson Hewitt Tax Service, franchise owner in Arkansas
Yvonne D. Kirkendall, co-owner, W. R. Kirkendall, EA
Frank L. Lanza, Director, Processing Services, California Franchise Tax Board

Business Working Group

Fran Bartlett (Chair), President & CEO, Federal Liaison Services, Inc.
Keith T. Dusenbery, Professor of Accounting and Information Systems, Johnson State College
Issac A. Nooe, III, Administrator, Information Resources Management Division, South Carolina DOR
Elizabeth M. Seymour, Vice President, Wachovia Bank, N.A
John A. Stauffer, Sr. VP of Product Planning, Ceridian Corporation/Ceridian Tax Service

Appendix D

Electronic Tax Administration Advisory Committee

Strategic Planning Recommendations & Review of:

Internal Revenue Service

Electronic Tax Administration

A Strategy For Growth

IRS Publication 3187
December 12, 1998

June 17, 1999

Contents

Executive Summary

The Electronic Tax Administration Advisory Committee (ETAAC) created under the 1998 Restructuring and Reform Act (RRA) is issuing strategic planning recommendations and a review of the first Internal Revenue Service (IRS) Electronic Tax Administration (ETA) Strategic Plan issued in December 1998. The comments have been organized to parallel the IRS-ETA Strategic Plan document.

The development of an ETA Strategic Plan in six months is a notable achievement. IRS must build on this good start by sustained effort to mature the strategic plan. A strategy which will achieve the goal stated in the 1998 RRA of having at least 80% of all Federal tax and information returns filed electronically by the year 2007 is not yet complete. The IRS-ETA strategic plan projects 49.4-70.4 million e-filed returns in the year 2007, which is short of the 80 percent goal by more than 20%. As ETA strategic planning continues to develop, additional initiatives will be identified that will improve IRS' ability to meet the 2007 goal.

ETAAC believes that the IRS and ETA must take the following actions to achieve the RRA goals established by Congress for 2007:

- Monitor the IRS strategic plan to ensure that it integrates and supports the ETA strategic plan, particularly in the information technology (IT) area.
- Document a process for identifying new projects, refining and assessing annual performance measures, and update the strategic plan to move toward achievement of the goals.
- Align ETA customer segments with the four business units now being established by the IRS organizational Modernization plan.
- Focus IT modernization upon electronic transmission of information and engagement of the private sector for solutions rather than improvement of paper processes.
- Make ETA initiatives a high priority in the IRS IT modernization so they are synchronized with major IRS modernization blueprints rather than competing for attention in later years. It is imperative that IRS ETA projects be integrated into the IRS modernization blueprint at an early stage.
- More aggressively advertise taxpayer and preparer benefits for e-filing. Effectively deliver and enhance such benefits to create taxpayer awareness and trust in e-filing.
- Continue to assign authentication, security, and privacy initiatives a high priority and continue to move forward quickly in this area. The 1999 filing season PIN and digital signature projects are major steps forward.

- Give ETA adequate resources and authority for pilots and prototypes that respond quickly to the rapid change in the electronic commerce marketplace.
- Monitor Electronic Return Originator (ERO) concerns to ensure that EROs perceive and receive benefits and incentives, which are greater than paper preparers. Handle suspensions in a timely and effective manner.
- Use the ETA strategic plan to articulate how partnerships with the private sector and other government partners such as states can be facilitated and supported. As the plan matures and additional initiatives added, continue identifying to the private sector which projects the IRS intends to undertake and which projects will be "released" to the private sector so duplicate resources are not wasted by private partners on IRS internal projects.

Overview

The Electronic Tax Administration Advisory Committee (ETAAC) was created as part of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA). The objective of ETAAC is to assist the IRS in meeting its strategic goals for electronic tax administration (ETA) by providing private sector and other external partners review, discussion and recommendations to the IRS in the development and implementation of its ETA strategic plan.

The RRA also required the IRS to develop an ETA Strategic Plan within six months of its enactment, and assigned the ETAAC the responsibility to report on the status of the ETA plans to Congress. This report serves two purposes: first, as a recommendation to the IRS, and second, as a component of the report to Congress.

In reviewing this strategic plan, ETAAC established simple evaluation criteria:

Is the plan complete?

Is the plan aligned with the rest of the IRS plans?

Does the plan contain the essential elements necessary to achieve the goals established by Congress?

The following comments and recommendations are offered constructively to this new foundation for the future.

To assist cross-reference, the following sections are organized with the same categories as *A Strategy For Growth.*

Introduction

Purpose

The IRS has made progress on ETA initiatives but more remains to be done. A strategy which will achieve the goal stated in the 1998 RRA of having at least 80% of all Federal tax and information returns filed electronically by the year 2007, and of having all returns prepared electronically filed electronically by 2003 is not yet complete. The IRS-ETA strategic plan projects 49.4-70.4 million e-filed returns in the year 2007, which the IRS recognizes is currently short of the 80 percent goal. As ETA strategic planning continues to develop, additional initiatives will be identified that will improve IRS' ability to meet the 2007 goal.

Progress to Date

The development of a strategic plan in six months is in itself a notable achievement. ETAAC recognizes that strategic plans of this nature usually take several update cycles to reach full maturity. The comments offered by ETAAC in this document should be used to guide future efforts at maturing the strategic plan.

The IRS has made early and significant progress in launching its effort toward achieving the goals. The following are noteworthy.

Established Baseline

As a baseline, the Plan shows the level of electronic transactions achieved in 1998:

- 24.6 million Form 1040 IRS e-file receipts in 1998.
- The successful pilot of the Form 941 TeleFile under which approximately 878,900 quarterly employment tax returns are expected to be filed in 1998, in addition to the 941,400 Forms 941 that are expected to be filed electronically by payroll service providers.
- 80% of all tax deposits are made using Electronic Federal Tax Payment System (EFTPS).
- 35 million downloads from the IRS Internet website.

The Strategic Plan also details expected performance and pilot projects to be implemented in 1999, which includes, much greater use of credit card payment of taxes.

Creative RFP-RFA Process

In 1998, private sector assistance with e-filing was creatively sought by soliciting it through Requests for Proposals (RFPs) and Request for Agreements (RFAs) that offered no fee, but encouraged private sector cooperation. As a result, credit card payments will be accepted in the 1999 filing season. The concept of cooperatively seeking free private sector ideas and services is new for the IRS and merits recognition for its creativity in enabling private sector linkages to establish services the IRS could not do on its own.

ETAAC encourages the IRS to continue the RFP/RFA process on an annual basis and incorporate it as part of its annual planning. ETAAC also encourages the IRS to coordinate this process, to the extent possible, to coincide with the development cycle for the private sector, to encourage the best possible participation and support by the private sector.

Making e-filing Beneficial to Taxpayers

E-filing currently provides many benefits to taxpayers and tax practitioners alike. E-filing is the only method of filing that provides acknowledgement from the IRS that the return was received and accepted, generally within 24 hours. Using the e-filing DIRECT DEPOSIT feature allows most taxpayers to receive their federal refund within two weeks of the acceptance date. Error rates for e-filed returns are far less than for traditional paper-filed returns. New in 1999, taxpayers e-filing balance due returns may pay their taxes by credit card or by direct debit to their checking or savings account. Yet with all of these incentives, many of which have been in existence for the past 12 years, e-filing has still only penetrated approximately 20% of the individual return volume. More incentives are needed to make e-filing the preferred way to file tax returns.

Since the individual tax return volume is almost evenly split evenly between taxpayer-prepared returns and tax practitioner-prepared returns, additional incentives are needed for each group. The most logical place to start is the tax practitioner group since the vast majority of tax returns prepared by tax practitioners are prepared on computer. Current obstacles will need to be overcome and more incentives will need to be implemented to meet the IRS 1998 RRA interim goal that states all returns prepared electronically should be filed electronically for taxable years beginning after 2001. Incentives other than monetary discounts may be effectively used for this group. The IRS-ETA has several projects in the strategic plan such as electronic account resolution that will help attract preparers to e-filing. The IRS needs to develop bundles of incentives to preparers to encourage them to convert to e-filing returns.

Since the IRS 1998 RRA goal for year 2007 is to reach 80% of all tax returns, much more penetration into the taxpayer-prepared group will also be needed. Many new incentives will need to be put into place for e-filing to become the preferred filing method for taxpayer-prepared returns. The IRS recognizes this in many of the proposed projects but these incentives will need to be effectively marketed to the preparer community to convert them to e-filing.

Signature Alternatives

In the 1999 filing season all 12 million taxpayers (8 million households) that prepared returns using computer software in 1998 received postcards with an e-file customer number (ECN). E-filing taxpayers, that use the ECN, will not need to send Form 8453. In addition, over 8,000 Electronic Return Originators (EROs) have been authorized to participate in a Personal Identification Number (PIN) project that permits taxpayers to enter a PIN at the ERO's office rather than sign and mail Form 8453. Additionally, experimenting with digital or PIN signatures prepared electronically has already begun in the 1999 filing season. Further development of signature alternatives is strongly encouraged.

Maturing the Initial Strategic Plan

The plan is introduced as a work in progress, and clearly states that changes to the plan, as well as the IRS' progress toward implementing it, will be highlighted in the ETA's annual report to Congress. Through this recognition, the IRS has achieved an important element to success — planning is a continual process in achieving the goal.

The commitment to ongoing revision and improvement of the plan bodes well for a more collaborative, engaging planning process. The public presentation and launch of the plan, as well as the solicitation of comments from all interested parties and stakeholders, represents a positive cultural change from past tradition.

To further amplify the importance ETAAC places on this, we recommend the planning process be refined by incorporating the following:

- Implement a process for continual strategic plan refinement with an annual revision to the strategic plan. Many elements of the strategic planning process are underway but have not been articulated in a formal way. We recommend IRS document its strategic planning process in the next update of the ETA Strategic Plan. The planning process should include the following elements.

- ♦ Internal efforts; such as, market research, technology assessment, issuance of ETA RFP and RFA (similar to what was done this past year), budgeting, and stakeholder outreach.
- ♦ Development of annual performance measures.
- ♦ Annual monitoring and assessment of the selected performance measures.
- ♦ Formal assessment of pilots implemented during the year.

- Annual strategic plan updates that adjust for past performance and introduce any necessary changes.
- Outline the process for creating operational plans that accomplish the strategies, tactics and projects in the strategic plan.

Articulation of the strategic planning process, including updates of the strategic plan, will demonstrate that the strategic plan is a living document, one that is adjusted to take results achieved and new experiences into account, and is adjusted with changes as needed.

ETAAC recommends ETA consider the creation of an ETA Operational Plan which would be separate from the ETA strategic plan and could be seeded by operational components currently within the strategic plan and add risk planning, budget, and additional marketing issue. The initial strategic plan is a blend of both strategic and operational items. The separation could bring greater clarity and focus to the strategic issues.

Summary

The ETA Strategic Plan has identified the high level goals of where the IRS must go and provides much more detail than required by OMB Circular A-11 (GRPA). The plan has identified key projects with stated timetables to achieve these goals. The plan charts a vision, with sufficient flexibility to adapt, as the Plan's on-going implementation brings greater perspective.

Mission, Goals and Key Strategies

Overview

The plan successfully articulates the ETA mission, vision and basic goals for "revolutionizing" how taxpayers transact and communicate with the IRS. We strongly endorse the IRS direction to take "…bold and innovative steps to revolutionize how taxpayers transact and communicate with the IRS…"

Presently, the plan places heavy focus on the electronic filing transaction. This focus is understandable, considering the congressional goal established for e-filing. As the plan matures, it is important to articulate the vision of how taxpayers will communicate with the IRS for electronic tax administration transactions other than e-filing.

Important identification and inclusion of key stakeholders and provisions of recent legislation were made in stating the goals.

Strategic Goals for 2007

The goals for 2007 represent a milestone for the IRS. The key milestone of achieving 80% e-filing is expressed as electronically transacting with 80% of the taxpayers. This is the key goal and is recognized as such. Equally impressive are the additional goals that focus on measuring quality and satisfaction.

ETAAC recommends a clarification of the 99% integrity and accuracy goal. With 1.2 billion tax and information returns, 1% represents 12 million returns. Differentiating between taxpayer inaccuracy and IRS transaction integrity is important. We believe IRS should aggressively protect transaction integrity and internal processing accuracy to a much better level than 99%. Taxpayer confidence can only be achieved if IRS manages transaction integrity and internal accuracy to a zero errors and loss basis goal.

Strategic Goal for 2003

The important goal, mentioned in the Introduction, of getting all returns prepared electronically to be filed electronically by 2003 (tax year 2002), is not addressed in the goals. Without a specific objective and corresponding operational plans, this goal will not be met. Further, ETA recognizes and ETAAC believes that the plans and projects that have been currently identified are not sufficient to achieve this goal.

Addressing Customer Segments

As part of an on-going effort to modernize its organization, the IRS has identified four business units into which it is reorganizing to better serve the diverse customer requirements — notably, the Wage and Investment, Small Business and Self-Employed, Tax Exempt, and Middle and Large Corporations. Because of the diverse needs of the customer segments and the profound impact the new organization will have on customer interactions, to the extent practical, future editions of the strategic plan should be organized around these customer segments with segment specific strategies. The ETA strategy for each business unit should be tailored to the taxpayers' needs without developing independent technical infrastructures.

Differentiated Service

As the business units begin operation, it is likely that the appropriateness of providing different levels of service for different customer segments will become clearer. The need to provide taxpayers with specialized services is highlighted in the goal to achieve their high level of satisfaction. However, there is another opportunity for differentiated service that is not addressed, but should be carefully considered — paper-filed vs. e-filed.

We recommend that the modernization efforts in products and services be focused on those that use electronic communications rather than invest in expensive improvements to the legacy, paper-based and paper supporting systems. This will permit the redevelopment and redeployment to concentrate on fully modernizing through electronic transactions. It is important to make the e-file method preferable to paper filing in all respects including taxpayer's perception of compliance checking of paper vs. e-filed returns. The paper-based systems should eliminate themselves, as taxpayers transition to electronic communications. Taxpayers must perceive clear benefits to e-filing versus paper filing. This approach will substantially improve the probability the 80% goal will be achieved by 2007.

Further, we recommend that all advantages of filing on paper over filing electronically should be eliminated. Here are two examples.

- Data is required on e-filed returns that is not required with paper returns.

This can be corrected by simply requiring the same information on paper as is requested for e-filed returns.

- Electronically filed returns are not accepted for filing (rejected) when the same return is accepted on paper.

To correct this disparity, paper returns with SSN problems, calculation errors and other problems could be return to the taxpayer with the appropriate correspondence, similar to the way e-filed returns are rejected. The processing of the return would not be continued until taxpayer response is received.

Market Opportunities

We agree with the assessment. The opportunity is there. The challenge "…is to develop product and services that are so simple, inexpensive and trusted that taxpayers will prefer these to traditional methods of calling and mailing." It is through the continual planning, initiative development and operational implementation that the opportunities will be converted to goal realization.

For example, new creative initiatives, such as expanding partnerships with other federal and state agencies to increase benefits of e-filing, should be continued and expanded. Marketing efforts are new to IRS and ETA has developed some excellent advertising approaches this year. Industry typically puts a lot of effort into evaluating the results of its marketing and advertising efforts, and ETAAC is encouraged that ETA has established qualitative and quantitative methods to evaluate the effectiveness of its marketing efforts.

Challenges

Technical Infrastructure & Competing Information Systems Priorities

Developing the technology infrastructure and information systems, required to support the transition to electronic business practices, is essential to success. The plan states that completion of the necessary systems capabilities to achieve the goals "…will be competing with other critical Information Systems priorities, including the extraordinarily complex tasks of Modernization and preparing for the Year 2000."

We recognize the challenge of the Year 2000 transition and were pleased to hear Commissioner Rossotti state, at ETAAC's December 1998 meeting, that the projects were well on their way to completion. ETAAC strongly encourages the IRS to synchronize the IRS strategic plan, the ETA strategic plan, and the Modernization plan into a cohesive set of documents with common goals, objectives and strategies for the IRS.

Product and Service Cost and Complexity

We strongly concur with the expressed view that IRS must simplify the e-filing system to make it more convenient and cheaper to use.

Taxpayer Suspicions

We believe that building confidence and trust in e-filing security of confidential information is a marketing challenge for the IRS and must be supported by marketing the benefits, successes and ease of e-filing.

Security and Privacy

Assuring and maintaining security and privacy are very important components of success. We endorse the PIN implementation as an interim and adequate solution, and recognize the efforts to moving toward PKI. However, because of this importance, we also believe the IRS should move more quickly to effect a solution.

Once a Year Opportunity to Implement Change

Viewing change as once a year opportunity must be put aside to meet the goals. Certainly the basic elements of the tax return filing have a once a year attribute. However, many opportunities of electronic administration do not. For example, account management systems, including taxpayer e-mail, could be piloted and implemented at any time. In developing new systems, architectures should be enabled that permit incremental updates at any time during the year.

Summary

Many of the significant challenges are identified and discussed. To implement the initiatives described in the strategic plan, the IRS is encouraged to develop an operating plan that details what will be done and assigns responsibility for implementing each initiative. Further, the IRS is encouraged to develop a planning process that promotes the establishment of new and innovative initiatives that will continue to contribute to the achievement of the goals.

Priorities

Achievements

The IRS has successfully recognized key themes to achieve the goals:

- The need for appropriate authentication and security.
- The need for modernized and upgraded technical infrastructure to deal with the increase in e-taxpayer number and e-tax return scope.
- The need to utilize distributor channel management to overcome the taxpaying public's lack of knowledge and enthusiasm as to electronic transaction capabilities.
- The need for renewed human resources internally, and partnerships externally, to bring about the necessary innovations and environment for change.

Initiatives have been launched in each of these areas. What follows is the need for the IRS to map out a precise operational plan to achieve its goals.

Account Management

The IRS ETA group is undertaking an innovative approach in working with the tax practitioner community. The account management approach being taken has been proven in the private sector and will be equally effective for the IRS. ETAAC fully endorses the customer-centric nature of the program.

The launch of the account management program is initially envisioned to include only those products and services under the direct responsi ility of the ETA group. We recommend the IRS evaluate expanding the scope of the account manager to include all practitioner interactions with the IRS — ETA-related or not — as a premium service for those practitioners fully supporting e-filing and willing to conduct business with the IRS electronically. Those practitioners choosing to remain predominantly paper filers should not be supported by this service. We believe the single point contact will result in greater satisfaction and effectiveness.

Technical Infrastructure

"Building the Foundation" identifies six areas as priorities for infrastructure development; these are Authentication, Processing System Consolidation, Performance Analysis, Internet Capabilities, Fraud Prevention and Control, and Annual Maintenance. These are important priorities, but ETAAC believes that other important items of equal importance must be added to the list. Some of these are:

- The taxpayer master file must be brought online.
- Correspondence must be modernized with electronic transmission.
- Account access must be enabled through Internet access for taxpayers, their EROs and other tax professional representatives,.
- Processing systems must be developed and implemented that will handle substantially higher volumes of transactions.
- Capabilities must be fully implemented to enable the filing of all types of returns with all of their forms and schedules.

The technical infrastructure development that is so critical to achieving ETA goals should be contained in the Modernization Blueprint, or other documents that IRS is using as operating plans. The following topics all affect the achievement of ETA goals, but fall outside of the control of IRS ETA organization; illustrating the high degree of support that ETA requires from other IRS organizations if ETA goals are to be achieved. These topics should be addressed in an IRS operating plan such as the Modernization Blueprint.

Topics for future operational plans:

- The strategies for completing the necessary technology development.
- The IT governance or establishment of mechanisms whereby the organization accomplishes its overall goals.

Although the current modernization plan makes a case for architectural principles, it provides only a series of guidelines. The timely introduction of a governance process that includes architectural principles and standards (information, data, application, technology and knowledge) needs to be addressed. The speed with which IT governance and new architectural standards can be introduced and approved will be critical to the success of any strategic objective identified by the plan, and needs to be addressed in the context of the technology infrastructure strategy.

- The new IRS organization forms four business units, supported by one technology unit.

  For all or each unit, achieving uniformity in the implementation of technology solutions across the business units should be an express goal. Permitting divergence will have a confusing and costly effect on taxpayers and the private sector partners.

- Obtaining commitments for the resources necessary to ensure that all projects will be complete in time to reach the goals.

  Conflicting priorities should be resolved in the early planning.

- Placing emphasis should be placed on the critical importance of an early implementation of the required systems.

  The current Modernization Blueprint shows two new functions essential for ETA, storage of up to 100 percent of digitized and electronically filed data and acceptance of 100 percent of the data from electronically filed returns. The IRS is implementing these functions earlier than planned in the prior blueprint. ETAAC endorses the early completion.

- Rapid identification, development, piloting, and rollout of new initiatives that take advantage of frequent technological change.

  The field of electronic commerce is a very dynamic world that is changing rapidly. The IRS needs to take advantage of these trends and developments and apply them to ETA. The recent addition of the Prime Contractor as an IRS resource allows the IRS to accomplish the rapid deployment of new initiatives that would have not been possible in the past.

Internet Capabilities

ETAAC strongly concurs with the IRS when it states “The IRS must position itself to take full advantage of the public's growing acceptance and use of the Internet.” ETAAC believes it is incumbent for the IRS to develop an inclusive strategy fully utilizing the Internet for doing business with individual and business taxpayer customers. Further, ETAAC suggests the IRS’ plans for bringing taxpayer account-related transactions to the Internet be set out in the operational plan.

Authentication

We are fully supportive of the initiatives the IRS has undertaken to solve the authentication, security and privacy issues. ETAAC is fully supportive of the alternative signature initiative undertaken by the IRS, including the use of PINs.

As the IRS evaluates alternate identification and authentication methods for the future, the IRS is encouraged to include a risk analysis that weighs compliance and potential fraud issues for a handful of tax cases against burden reduction for the millions of taxpayers who file electronically.

We suggest the following questions be answered.

- Security and privacy — what are acceptable levels with e-filing?
- Signatures and authentication — with e-returns, what is the level of certainty that should be required?

Standards Adoption

The IRS has not adopted and the strategic plan does not address the adoption of standards for electronic transactions (tax returns, information returns, correspondence, account information, etc.). To facilitate the broadest adoption by taxpayers and potential private sector partners, appropriate national and public sector endorsed standards should be adopted. We believe this should be addressed at the strategic level.

Marketing Services

In presenting its marketing plans, the IRS demonstrates that it recognizes that marketing utilizing distributor channel management is an important component of success. ETAAC fully supports these efforts. Unique marketing to different segments of the filing community is identified. We also believe this is the appropriate approach. As the plan is more fully developed along the four major taxpayer segments, so will the unique marketing message for each segment become more crystallized.

The need to market to businesses should be further developed in future editions of the plan.

Questions have been raised if the spending is sufficient to attract enough attention to induce sufficient numbers of filers to change their method of filing. As the results of current marketing and advertising efforts are evaluated, consideration should be given to increasing these efforts if they prove effective.

Management Improvements

Private Sector Partnerships

Clear recognition is given to the importance of strategic partnerships. "In order to revolutionize Electronic Tax Administration, it must embark on a new stage in its relationship with external stakeholders to formulate a broader strategy for electronic service delivery that builds products and services through partnership with private industry." The plan sets a new tone and realigns the way in which the ETA section of the IRS is conducting business, particularly utilizing the RFP-RFA process to enter into six non-monetary agreements for enhanced taxpayer service during the 1999 filing season. This is an important redirection towards a more successful outcome, in both the perception and taxpayer satisfaction of the agency, as well as to create a more responsive, flexible environment for ongoing improvements. While ETA has made a notable start in establishing private sector partnerships, we believe that future editions of the strategic plan should be expanded in the partnership area to encompass the following.

- Expand the techniques used to achieve additional partnerships with the private sector that enable e-filing.
- Continue to address the role the software industry, tax processor and preparer community are envisioned to be asked to play in the implementation of the strategic plan and initiatives.
- Clarify which projects the IRS will complete. Specifically, which projects:
    - will be undertaken internally by the IRS at taxpayer expense
    - will be contracted to the private sector, at taxpayer expense
    - will be left to states and the private sector and their investments.
- More fully describe the evolving mechanisms, for identifying new projects for pilot implementation and evaluation.
- Expand and build upon existing federal and state government sector partnerships.

Electronic Information Services

ETAAC is fully supportive of the continuing initiative for the IRS to publish via the Internet. Further, we believe the Internet is the electronic communication choice for the future. All future IRS customer services should be enabled through the Internet providing access by taxpayers, EROs, and other representatives of the taxpayers.

Other Considerations

The following topics were not directly addressed in the ETA strategic plan. We believe that each of these will add value by inclusion in the IRS plan.

Aligning ETA and IRS Strategic Plans

- It is essential that the ETA strategic plan be integrated into the IRS Strategic Plan as it evolves, particularly from an information technology perspective.
- The IRS is dividing into four business units: (1) Wage and Investment (to include ETA), (2) Small Business and Self-Employed, (3) Tax Exempt, and (4) Middle and Large Corporations. ETA will be housed in the Wage and Investment Unit. The IRS' stated intent that all other business units will continue to be adequately served by ETA appears appropriate at this time yet should be monitored in the future to ensure it does not impair ETA's effectiveness to achieve its strategic goals.
- Adequate resources for the projects required to make the transition to electronic administration by 2007 are not addressed. We believe it is important for the IRS strategic plan to commit to providing sufficient resources to ensure the necessary systems and services will be implemented on the required schedule. Further, identifying a multiple year resource plan and budget would be a valuable tool in assisting achievement of the overall goal. This latter element could effectively be contained in an operational plan.

Clarifying the Plan

- The IRS should develop a vision of how taxpayers will interact with the IRS as a result of the implementation of the strategic plan direction. This vision should describe how information will be electronically presented, transmitted, received, routed, acknowledged and accessed by individuals, businesses, and their representatives. This material may be too detailed for the strategic plan, but having such a documented vision should be part of IRS' overall plan. The material may be well suited for a Concept of Operations.
- An important element of the plan is the implementation of the various initiatives. The plan contains comprehensive time lines for each project; however, there is no discussion of the operational steps, major segments and overall timing. As noted earlier, having such information is the next step in implementation.

Confirming Objectives Will Be Achieved

- There is a general consensus within ETAAC that the strategies, as presently articulated in the plan, need additional focus and resources to lead to achievement of the goals. The recognition of the huge market opportunities is extremely foresighted. Therefore, we recommend that future editions of the strategic plan contain additional planning and plan developments in order to meet the goals for 2007.

- Convincing individuals that prepare their returns manually to switch to an electronic method will be a slow cultural change. The plan currently leaves the implementation of business tax returns (corporate and partnership income tax, and the information returns prepared by them) until later in the implementation period. We recommend the initial emphasis be placed in two areas.

  - Getting those returns prepared electronically filed electronically.

  - Getting corporations and partnerships to file electronically.

  Many businesses already use computers, and would quickly embrace electronic filing. However, more attention is needed in the plan to the needs of businesses, and marketing efforts should be implemented to induce them to make the transition.

  Overall the ETA strategic plan places emphasis on the e-filing of the 1040. Coverage should be extended to other large volume returns, including corporate, partnership, and information returns at the same level of commitment.

- Quantitative survey data should be obtained supporting the hypothesis that the identified strategies and projects will achieve the projected results and goals. This data should be used in the process of preparing the plan, measuring appropriate references within the plan. The private sector may be in a position to contribute data as well. The IRS should invite the private sector to make data available where it might be helpful. To the extent possible, private sector data should be gathered and used to correlate and substantiate the research findings of the IRS.

- More specific quantitative and intermediate milestones should be incorporated into the plan—quantitative goals for each year that lead to achievement of the objectives in 2007. These intermediate targets for every year will provide the IRS and stakeholders a straightforward method of verifying the implementation is on-track to achieving the ultimate goal.

  Many goal measurements can only be measured annually; however, this is a long time to examine progress. To the extent practical, quarterly progress reporting should be endorsed.

- As part of an operational plan, the strategies, tactics and plans that are in support of the strategic objectives should be presented and substantiated to convincingly establish the strategic objectives will be achieved.
- The tables in Appendix E do not show the complete picture. These tables only show electronic returns, and do not include total returns. Since the goal is expressed as a percentage, total returns should be shown as well. In addition, if all returns are shown, the table should include data on additional forms such as the 1120 and 990 that are not filed electronically at all. For example, the text on page 12 of *A Strategy for Growth* discusses return types that are not shown in the tables.

This list is not all-inclusive, but indicative of typical issues.

Critical Obstacles & Enablers

There are a number of obstacles and enablers that have sufficient importance that they rise to the level of strategic planning. We suggest that the following be added to the strategic plan.

- Document retention — what is the direction and proper guidelines for electronic and not paper retention? Do regulations or statutes need to be amended to endorse electronic document retention?
- All Forms & Schedules for All Returns — tax and information
    - The need to support all or most forms and schedules with electronic filing has been asserted as one of the most common reasons for not adopting e-filing. If the e-filing of all or most forms and schedules are not supported until 2003, it is unlikely that the goal of e-filing all forms prepared electronically will be achieved in that year. Accelerating this schedule is essential.
- New tax laws — New tax laws, because of their complexity or effective dates, may have a significant impact on tax software providers, tax preparers, and the IRS to be able to electronically process tax and information returns. This could hinder accomplishment of the legislative goals of the 1998 RRA. An example of this in the 1999 filing season is that taxpayers formerly eligible to telefile can no longer do so due to the new education credits and telefiled returns have declined from prior year levels.
- EROs are held to higher standard — ETAAC recommends the IRS eliminate the disparity whereby preparers filing electronically are held to a higher standard than those filing by paper and mail. Similarly, the preferential treatment given to paper returns over those electronically filed should be eliminated. Examples of this are the suitability requirements and suspension practices for EROs that are not required for those filing only on paper.

Non-Circular 230 preparers are motivated to remain with paper filing because they avoid the requirements placed on EROs and Circular 230 preparers. Not only is this major segment of the preparer population incented to avoid electronic filing, they also have no standards for exercising due diligence. We encourage the IRS to address this issue.

Appendix E

The Effects of Electronic Filing on Business

The Effects Of Electronic Filing On Small Business And Self-Employed

The mission of electronic tax administration, as stated in *A Strategy for Growth,* is to “revolutionize how taxpayers transact and communicate with the IRS.” There is probably no taxpayer segment more interested in seeing a “revolution" in how it must interact with the IRS than small business. At an April 1999 Senate Small Business Committee hearing on "Small Business Tax Filing Burdens", the US General Accounting Office identified over 200 requirements and their accompanying forms and schedules in the Internal Revenue Code (IRC) that could potentially affect small business.

Electronic tax administration likely will be beneficial to small business by simplifying compliance with IRC requirements. Convincing small business owners that electronic filing is beneficial will involve improving communications and enhancing the credibility of existing electronic systems.

Communications
The ETAAC recommends that the IRS focus on improving communications with small businesses to help them understand compliance requirements. At the April Senate hearing, several witnesses stated that many small businesses learn the rules of tax filing and record keeping requirements through penalties. Only when they are penalized for not meeting requirements do many small businesses actually understand what those rules are. The IRS already is taking positive steps to improve outreach to small business, including creating a unit, as part of its reorganization, that will manage all small business interactions with the IRS. The Small Business and Self-Employed Operating Division will handle everything from education to compliance for small business, creating a group that will have greater insight into the specific needs of and challenges faced by these taxpayers.

Marketing and communicating the benefits of electronic filing will help small business understand and become comfortable with new electronic filing services. The IRS announced in April 1999 several initiatives with the Small Business Administration (SBA) where the SBA will help communicate tax information to small businesses. The IRS also has begun a marketing effort for e-filing and is partnering with software manufacturers and tax preparers to improve access to electronic tax products and services. Building on these public and private sector partnerships would provide small business with more access to information and a better understanding of new initiatives and requirements.

To expand its use of the Internet, the ETAAC recommends that the IRS expand its online information providing small business owners with one place to find factual and educational material on their compliance requirements. The presentation of the material should be more than a publishing of the pertinent regulations, but a user-friendly guide for the small business owner.

Electronic Federal Tax Payment System (EFTPS)
A Strategy for Growth states that "As taxpayers become more comfortable and satisfied with a specific aspect of electronic tax administration, the more likely they will also begin using other products and services as well." The US Chamber of Commerce and the National Federation of Independent Business recommended some changes to the electronic tax payment system, EFTPS, that would enhance the integrity of that system. While the new upper threshold limit makes EFTPS voluntary for more taxpayers (those with aggregate federal tax deposits below $200,000), many small businesses are not exempt. The ETAAC believes that the following changes would make EFTPS more user friendly:

- The IRS should improve taxpayer notification by providing timely notice to small businesses if they are required to use EFTPS before penalties are imposed. If an EFTPS-mandated taxpayer inadvertently makes tax payments by another payment method, a warning/"first time" notice should be issued in a timely manner and before penalties are imposed.
- The EFTPS avoidance penalty should be re-evaluated. Taxpayers believe that the ten percent penalty is excessive, considering that they have paid their taxes on time, just not through the required method, particularly if the problem has not been habitual.
- Small business also remains concerned that IRS and its Treasury Financial Agents through EFTPS may have access to their bank accounts. Improved communication and assurances that this is not the case would be beneficial.

Successfully transacting and communicating electronically with small businesses will require greater effort by the IRS to understand the challenges small businesses face in complying with a myriad of tax regulations and transaction requirements. The ETAAC believes the proposed IRS reorganization will focus more on understanding taxpayers' needs, which will help design other electronic tax administration initiatives. Ready access to products and services and better communication will demonstrate to small businesses that electronic tax administration is the preferred and most trusted means of interacting with the IRS.

The Effects of Electronic Filing on Large and Mid-Sized Business

Large and mid-size businesses are some of the most prodigious and most advanced users of sophisticated technologies. As such, their electronic tax administration needs are different than other taxpayers. Large and mid-size businesses have led the way on electronic payments of taxes and electronic filing of information returns.

There are at least six specific areas of electronic interface with the IRS by large and mid-size businesses:

- Business income tax returns
- Information returns
- Retirement plan requirements, including 401(k) plans, defined benefit plans, and profit sharing plans
- Electronic records retained by taxpayers for audit purposes

- Electronic payments
- Electronic communications

Business income tax returns
The current IRS plan for electronic filing of corporate income tax returns is to permit such filings in 2003. System constraints and a focus on individual income tax returns have caused the target date for implementation to be deferred. However, because large and mid-size businesses are early adopters of technology solutions, the IRS should consider accelerating the date for accepting electronically filed corporate income tax returns. Additionally, the cost of compliance with business income tax requirements is extremely burdensome. The opportunity to reduce this cost burden through electronic filing is a more powerful incentive than mandates, which should be avoided.

Information returns
Approximately 70 million taxpayers receive information returns from large and mid-size businesses. The information on these returns has traditionally been sent to the IRS via magnetic media. Although this method has satisfied the regulations of the Internal Revenue Service, technological advancements have made electronic data filing via automated transmission more inviting. Electronic filing via transmission will allow for direct network to network communication. This process will not only be more efficient, but less costly. Notification of taxpayers electronically should be enabled.

Retirement plan requirements
In order to provide security for retirement plan funds, ERISA and tax laws place significant burdens on large and mid-size businesses to effectively and properly administer various pension plans. As required by the Taxpayer Relief Act of 1997, the IRS has issued a Notice and proposed regulations allowing the use of electronic technologies to satisfy various notice and administrative retirement plan processes. The IRS has been responsive to comments by large and mid-size businesses and the IRS' guidance to date represents a positive effort to recognize the importance of electronic technology in present and future plan administration. Because electronic technology in this area provides tremendous cost savings to employers and serves to increase retirement plan coverage for employees of large and mid-size companies, IRS guidance should further expand and improve permitted uses of technology in retirement plan administration.

Where electronic technology is allowed, the ETAAC recommends that duplicative paper notices and communications should not be required if plan participants are not unreasonably disadvantaged. Requirements for the use of technology in this area should not be more stringent than requirements for older methods of plan administration. Many forms filed in conjunction with retirement plans require an employee's signature, and the ETAAC recommends that electronic signatures be allowed. Additionally, the filing of tax returns, such as Forms 5500 and Forms 1099-R, should be enabled and allowed in electronic format rather than in paper as currently required.

Electronic records
Large and mid-size businesses must maintain enormous quantities of data to support their tax returns. The IRS has generally been supportive of preserving that data electronically. However, new technology may present new challenges in archiving and retrieving data. The IRS needs to continue to work with taxpayers on a regular basis to be certain that data archiving and retrieving processes are adequate for IRS needs while keeping in mind practical considerations of the taxpayer, such as the cost of these processes. Additionally, taxpayers should not be required to retain data that is not necessary for an audit nor should this data be stored for any longer than is necessary. The IRS should also continue efforts to close audits as rapidly as practical so that data storage and retrieval is minimized.

Electronic payments
Large and mid-size businesses pay billions of dollars in corporate income taxes and withholding taxes from employees. Last year, the IRS collected in excess of $1 trillion electronically. This is an incredible success story, but the IRS must remain vigilant about using means that are inexpensive, readily accessible and secure. As technology continues to evolve in this area, the IRS must also continue to make progress in implementing this new technology.

Electronic communications
Large and mid-size businesses are among the most sophisticated users of electronic communications. The IRS has made some significant advancements in communicating with taxpayers. In particular, the IRS web site receives millions of "hits" and is an effective tool to distribute information.

Electronic communication is important to taxpayers, particularly the ability to download tax forms. The ETAAC is encouraged that the IRS has identified initiatives to improve electronic communications with taxpayers in *A Strategy for Growth*. Large and mid-sized business taxpayers, as well as other taxpayers, should be able to correspond routinely with the IRS via e-mail. E-mail correspondence can be more efficient and allow for greater service to taxpayers in meeting their tax obligations. Furthermore, unlike oral conversations, e-mail has the potential to provide taxpayers with written correspondence sufficient to avoid certain tax penalties. At the earliest possible time, e-mail from the taxpayer to the IRS, particularly in response to an IRS Notice, should be implemented.

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