

**STATEMENT OF
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ON THE COST OF TAX RETURN PREPARATION
SENATE COMMITTEE ON FINANCE
APRIL 4, 2006**

Thank you for the invitation to comment on the tax filing season from the perspective of a participant in the Free File Alliance. My testimony reflects only H&R Block's experience. Free File Alliance management has submitted a separate statement for the record.

The landscape of tax return preparation has evolved in significant ways since enactment of the IRS Restructuring and Reform Act of 1998. Let me highlight three ways it has changed:

Electronic Filing and the Free File Alliance

First, electronic tax preparation and filing have become commonplace.

Over 80% of returns are now prepared on a computer using tax preparation software, and over 50% are now e-filed. Do-it-yourself tax preparation, assisted by software, is growing, up 17% so far this year, for example. But the majority of e-filed returns come from paid and volunteer return preparers. At H&R Block, 95% of tax returns prepared at our offices are e-filed.

While America will fall short of the 80% e-filing goal set by Congress in the 1998 Act, steady progress is being made. We suggest Congress extend the goal to 2011, as the IRS Oversight Board has recommended, to maintain enthusiasm and remind us of the benefits of e-filing.

Filing channels are no longer rigid. At H&R Block, clients can visit one of 12,000 offices; or fill out an organizer worksheet online and submit it to a tax pro; or start online and access a tax professional by phone; or transfer the return to an in-office tax pro for help. Taxpayers can be served conveniently, in blended ways, when and how they choose.

One innovative channel is the Free File Alliance, initiated in 2003 and recently renewed through 2009. It is an agreement between the IRS and the tax software industry to provide free federal income tax preparation and online filing for low- and moderate-income Americans. Since its inception, over 14 million returns, including 3 million so far this year, have been filed. This public-private partnership today involves 20 companies. Taxpayers have saved over \$42 million through this donation of services.

The first Free File agreement built on the tax software industry's voluntary provision of free services. It was intended to broaden eligibility to 60% of taxpayers. The renewed agreement, signed in 2005, expands it to 70% this year, or 93 million tax filers with adjusted gross incomes of \$50,000 or less. The product offered is the same as available commercially, not a stripped down version, and Free File standards exceed government regulatory requirements.

Free File is proving itself a winner for taxpayers, for the IRS, and for tax software providers — an example of cooperation and partnership in the public interest.

Paid Tax Return Preparation and Financial Education

Second, at the same time, Americans are increasingly turning to paid professionals for tax assistance.

About 60% of all taxpayers and about 70% of applicants for the Earned Income Tax Credit use a paid preparer. Their reasons include not only dealing with tax complexity but also convenience and the opportunity to receive financial education and counseling.

There is increasing recognition that tax time is an opportunity for an annual financial check-up. With nearly 80% of taxpayers receiving a refund averaging over \$2,100, there is both a teachable moment and an opportunity to save for a family's key financial goals of college, homeownership and retirement, using tax-advantaged vehicles like the Retirement Saver's Credit.

In addition, we use the opportunity to alert low-income clients to their eligibility for a variety of government benefits that can improve their family's finances, including children's health insurance, food stamps, and prescription drug discounts. Our Free File offering also provides this information.

Fees vary by location and are based on the forms filed and the work done, not on a client's income or the size of his refund. They can be as low as \$24 for the simplest 1040 EZ. This year they average \$154 for a federal, state and any local return at H&R Block offices as of March 15. This compares favorably to fees charged by many competitors.

Better Regulation and Enforcement

Third, the need for meaningful minimum quality standards has grown.

The IRS has said, "The vast majority of return preparers are honest and reputable." We agree. But consumers who pay for help deserve some assurance of competence.

Thirty years ago, Henry Bloch proposed IRS registration of all paid tax preparers. We renew that call today and go further. We believe IRS certification of paid tax return preparers — which would require validation of applicable tax knowledge, criminal and tax-filing background checks, and minimum levels of continuing tax education — would benefit the public.

This could be accomplished through enactment of section 4 of S. 832, cosponsored by Chairman Grassley, Ranking Member Baucus, and other members of the Committee, which would require testing for technical knowledge, competence and ethics, continuing education, and stiffer penalties for misconduct.

We support enactment. Taxpayers deserve the highest standards of competence and integrity from the tax preparation industry, standards we believe we currently meet.

The new program would complement existing regulation. All preparers today are subject to laws covering fraud, negligence, diligence, misrepresentation and unauthorized disclosure, and can be enjoined from misconduct. Practitioners who represent taxpayers before the IRS on post-filing issues — attorneys, CPAs and Enrolled Agents — are regulated by IRS Circular 230. And there are extensive additional rules to cover Electronic Return Originators.

Because 80 million taxpayers pay for help from over a million tax practitioners in a compact 10-week period, effective enforcement requires adequate funding and staffing. We applaud the IRS's recent increase in investigations of return preparers and upgrading the Office of Professional Responsibility. But the overall record in recent years shows room for improvement. We strongly recommend stepped-up IRS enforcement.

Training, Quality Control, Ethics Requirements

Competence depends on training and continuing education, especially given frequent changes in the tax code.

The average H&R Block tax return preparer has over 225 hours of training and nearly half have 5 or more years experience. Our tax professionals, at a minimum, must take our basic 66-hour tax course, with equal amounts of homework, and receive a passing test grade to be eligible for hiring. To be rehired, they must take at least 24 hours of continuing education each year. We offer 59 advanced courses. Our tax professionals are also trained on systems, products, policies and procedures, which require an additional 20-35 hours in class. Over 5,000 are Enrolled Agents or CPAs.

We have a strict “Code of Business Ethics and Conduct,” and must meet the due diligence requirements of tax return preparation and privacy standards in IRS rules. Our Electronic Return Originators require IRS approval, which may include FBI background checks, tax compliance verification and credit checks.

Our tax professionals work with a state-of-the-art computer program that checks calculations, theory and accuracy. There are approximately 10,000 diagnostics in our software that warn tax professionals that there may be something to review, error diagnostics that won’t let the user file unless they are corrected, and other diagnostics that check all IRS error codes. We also utilize a second review by another professional for many tax returns.

Our professionals have back-up at headquarters: Information Technology, Tax Research and Training groups provide support including on-demand help and customized research of complex tax questions. Our Compliance Department performs field reviews.

With a complex tax code and 16 million returns prepared in our offices by over 100,000 return preparers, occasional errors are possible. However, we believe our error rate at that volume level is small as compared to competitors or other professions. For all clients, we stand behind the quality of our work and guarantee that we will pay any interest or penalties if we make an error on their tax return. And we guarantee client satisfaction.

Our training and culture are clear on one critical point: We play it straight. Our interpretations of the tax code are grounded in solid research. We assist our clients in determining their correct tax liability to pay precisely what they owe, no more and no less.

Mr. Chairman, for over a half-century, H&R Block has built its reputation as the trusted tax advisor to Middle-America, and, more recently, as a tax and financial partner to our clients. Our best practices and code of ethics reflect a longstanding commitment to integrity and professionalism, which we renew today.