Wolters Kluwer Tax and Accounting
Statement Presented to the IRS: Real Time Tax System
January 25, 2012

Wolters Kluwer Tax and Accounting ("TAA") appreciates the opportunity to speak before the IRS and other members of the tax industry on the Real Time Tax System proposal. I am Dave Olsen, Director of Product Management at CCH Small Firm Services (one of the Wolters Kluwer Tax and Accounting business units). Wolters Kluwer TAA is the producer of tax compliance products for tax practitioners including ATX, TaxWise and CCH ProSystem fx Tax. In addition, the CompleteTax self-preparation product is provided to taxpayers. Wolters Kluwer TAA facilitates the electronic filing of 30 to 40 million tax returns of all types annually. We were a key driver of 1040 MeF volume for filing season 2011 with over 50% of the paid professional prepared 1040 MeF volume being transmitted through our compliance products.

As a software company, a key objective is to reduce both tax practitioner and taxpayer burden with efficient tools to support the tax compliance process. Real time data availability and validation has the potential to eliminate many post-filing burdens for taxpayers, tax practitioners, and the IRS. As the facilitator of many electronic interactions between these 3 key stakeholders in the return filing system, a primary focus for software developers is to provide solutions which increase efficiency and improve accuracy within the voluntary tax compliance cycle, while easing the challenge of constantly increasing complexity in the US Tax Code.

Approaching the concept of a real time tax system includes the acknowledgment of the challenges as well. Understanding and evaluating these challenges is critical to ensuring the success of a large scale change that will have a far reaching impact on the tax ecosystem. Challenges we foresee include: 1) Timing Challenges; 2) Identification and impact analysis of all stakeholders; 3) Creation of tools and processes.

Two underlying premises should also be identified:

1. The tax code we collectively operate under is complex, and reporting obligations can be significant and overlapping. Tax simplification is a separate issue that could impact some of the factors discussed, but for this topic the current tax code is assumed.
2. The principles of the voluntary tax system are assumed, under which the taxpayer submits what he/she represents to be the correct calculation of tax obligations. Systems and processes are thus assumed to support the taxpayer's chosen method of carrying out that compliance responsibility.

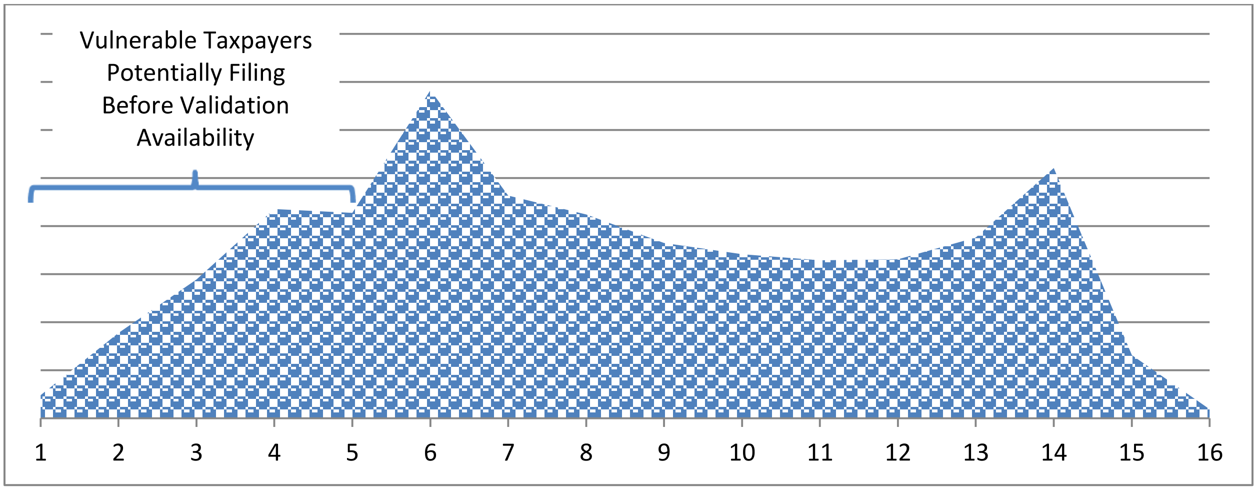
<u>Timing Challenges</u>

There are various timing challenges to be taken into account. Each manifestation of the timing challenge carries a different impact.

1. Filing deadlines – The timing between the deadlines for filing of various information returns and the April 15th tax compliance deadline significantly narrows the timeframe in which an extraordinary amount of work product has to be completed. The alternatives to narrowing this timeframe are to have earlier deadlines for information returns or a later deadline for income tax returns. The potential impact to adjusting the filing deadlines are:
   - Information returns: increasing speed without sacrificing accuracy
   - Income tax returns: refund delivery (see below)
2. Issue resolution – Issue resolution on these mismatches is currently done post-filing season. Moving these tasks to in-season activities creates additional burden on the tax practitioner community as well as unanticipated delays for the taxpayer. Since approximately 60% of taxpayers use a paid preparer to fulfill their tax filing obligations this is a significant amount of work that is being shifted to an already busy time of year.
3. Refund delivery – Many taxpayers depend on receiving their refund during January and February in order to fulfill financial obligations. Both the timing of the availability of an up-front validation system and issue resolution on immaterial mismatches could cause delays that create significant financial challenges for many taxpayers in need, including those counting on refundable credits. Historic e-file trends demonstrate that a significant number of taxpayers that receive refunds file as soon as the IRS begins processing in mid-January. Even a small shift of a couple of weeks could have a significant impact on the financial situation of these taxpayers.

These multiple timing challenges put together require an evaluation of whether the current process flow and filing deadlines are achievable under a real time tax system. As noted, a significant portion of filers submit their returns during the early season period. Even with accelerated information return submission dates which have been suggested, there are significant questions as to whether the data could be processed and available for up front validation without imposing delays on these vulnerable taxpayers.

Representative Filing Season Volume Pattern



Identification and Impact Analysis of all Stakeholders

A real time tax system would be a change in process across all aspects of the tax ecosystem changing many behaviors and processes that stakeholders are accustomed to. While change is a reality of the technology driven world we live in today, the success of all large changes requires understanding the depth and impact of the change to all stakeholders. An effective change management action plan must be in place in order to attempt to mitigate issues, minimize impact and allow for quick resolutions to unanticipated issues that arise.

Stakeholder Perspective – Small Business and Practitioners serving them:

While 155 payers make up 60% of all information returns filed, the IRS identified there are a total of 9.1 million payers. Many require assistance from full-service small accounting firms that represent the millions of small businesses that have both information return and income tax filing requirements.

In preparing this testimony, we talked to some of our customers to understand their perspective. One of the small firms made the following statement:

"We already juggle the intensity of multiple filing deadlines during the months of January – April 15th in order to keep our clients compliant. To shift post-filing activities to occur in these 3.5 months would be impossible for us to pull off without one of the contributing factors changing to facilitate the availability of time. "

<u>Creation of Tools and Processes</u>

The successful deployment of an initiative of this size will take the identification, development, and deployment of the right tools and processes with the input of stakeholders, subject matter experts, and input/analysis of industries that have successfully implemented similar processes. A review of recent initiatives shows that the creation of the right tools to support a new component of the tax system reduces error and backlog on the backend to ensure a successful initial return submission. (Examples include: Making Work Pay Credit and First Time Homebuyer Credit lookup tools)

What are the opportunities to evolve the tax system to be more real-time in the short-term?

The short-term starts with identifying all stakeholders and defining the process(es). Time must be spent in the requirements gathering and studying of processes already in place in the tax industry and other industries. This process will provide an understanding of what systems need to be in place. There are potentially 3 categories of systems that will need to be identified: 1) Existing systems that need to be modernized; 2) New systems that will need to be created; 3) Synchronization of new and/or existing systems that will have to interact.

After the processes have been identified and created launch a pilot program targeted at simple, specific demographics. For example: taxpayers with only the most common information returns as their source of income. The pilot program could be stepped-up to onboard additional taxpayer’s when an acceptable level of success has been achieved. In pursuing this objective, leveraging existing innovations brought forward by industry should be a primary objective, such as exploring how to make consistent and better use of information return data already being made available to recipients electronically. If the stakeholders agree on an objective, there may be efficient “steps in the right direction” that are possible even with government budget constraints.

A longer term goal should be the ability to validate return data before submission by the taxpayer/tax practitioner. While information returns only make up a portion of the details on a tax return, the ability to match against source data being provided to the IRS would provide a reasonable assurance that the information returns reported by the taxpayer are as expected and would not receive a mismatch error. This could reduce the amount of time that the taxpayer/tax practitioner will spend trying to gather all documents to complete the rest of the tax return. A key issue again revolves around how to leverage existing systems to capture the data and minimize the effort of developing a new process.

Operating an up-front matching process: What are the roles of the taxpayer, tax practitioner, and software industry to resolve issues?
The identification of high-level responsibilities can be assigned to stakeholders. However, without identified processes, the details of those responsibilities are conceptual. For example:

Taxpayer – receiving notification of error and providing data to resolve; interaction with information return payer, IRS and/or tax practitioner

Tax practitioner – receiving notification of error, gathering data to resolve error, balancing workload to provide timely resolution

Software industry – build intermediary communication bridges between taxpayer/tax practitioner and the IRS, Delivery of multiple electronic notifications (mismatch error, error resolution, error dispute, error acceptance)

Information Return Payers – Timeliness of initial reporting and error resolution

What tools could the IRS provide to support up-front issue resolution? How would the process work between the IRS, taxpayers, and practitioners to resolve issues up-front rather than after the fact?
Keeping processes on the front-end of the return submission will maximize efficiencies for both the taxpayer and the tax practitioner and ultimately result in smoother return processing for the IRS.

Up-front data validation – will allow the identification of all data the IRS is expecting, allowing the taxpayer/tax practitioner to either:
- Gather incorrect, incomplete, or missing information more timely.
- Provide explanation for the incorrect, incomplete, or missing information with the initial return filing.

Margin of error – An acceptable margin of error should be identified to prevent immaterial mismatches stopping a return from being processed.

Communications of criteria for return processing:
- This allows software developers to build additional functionality to warn taxpayers/tax practitioners of a return that will not pass IRS processing systems. Examples currently in place are the e-file reject codes, validations, and business rules. Software developers

have built functionality that increases the accuracy of the return for first-time acceptance by the IRS.

- Determining the status of a return that has a mismatch. Initial consensus indicated that a return should not be rejected. However, the status of a return that has a mismatch and required action must be determined and clearly communicated.

What issues and concerns should the IRS consider?

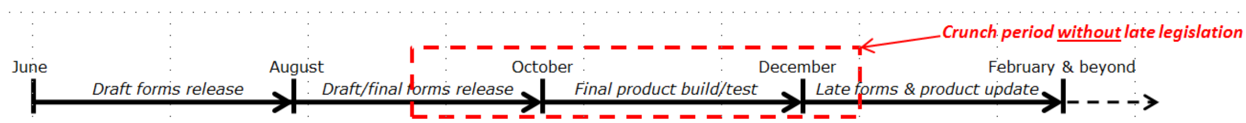
There are past "lessons learned" that should be considered when implementing a new filing process.

Accuracy of master data – The highest return rejects occur for master file mismatches (legacy e-file series 500 rejects). A subset of these rejects as a result of inaccuracies in the master file and may require taxpayers to ultimately file a paper return. The level of assurance in the accuracy of the master file must be relatively high. For those mismatches that the taxpayer maintains are in error, there must be a resolution mechanism to push the return through processing.

Refund release – Delivery of timely refunds must not be hampered by inaccurate IRS data or immaterial differences. According to the National Taxpayer Advocate Taxpayers Nina Olsen's recent annual report to congress she noted "automated processes are inherently imperfect, so the taxpayer's return position often turns out to be correct." This puts focus on the fact that the taxpayer's return filing experience must be preserved.

Taxpayer education – Taxpayer education is key; however outreach to impacted taxpayers can be difficult. A change in process and expected behavior creates confusion that must be managed and will be felt by all stakeholders that have interaction with taxpayers.

Late legislation – The trend of the past decade has shown that late legislation has almost become an expected factor in tax season. A piece of late legislation that impacts a component of upfront matching must be anticipated and mitigation plans created to minimize the impact. The impact of late legislation can create confusion in the filing process, as we saw in filing season 2011 with the delay of certain returns being accepted. While an up-front validation process has attractive elements, reliance on such a system adds another risk factor to an already challenging process of "delivering tax season".



The creation and implementation of a real time tax system would have benefits to the filing process, but in exchange would require a significant investment of time and resources to ensure the success. Careful analysis would be required to determine that the final goal is achievable and creates enough benefit to offset the cost. The tax industry has identified, tackled, and addressed many challenges in the past; we look forward to continuing to identify opportunities for the real time tax system.