

DEPARTMENT OF TAXATION

2010 Fiscal Impact Statement

1. **Patron** Kathy J. Byron

3. **Committee** Senate Finance

4. **Title** Virginia Free File Program

2. **Bill Number** HB 1349

House of Origin:

☐ **Introduced**

☐ **Substitute**

☐ **Engrossed**

Second House:

☒ **In Committee**

☐ **Substitute**

☐ **Enrolled**

5. **Summary/Purpose:**

This is a "Section 1" bill that would require TAX to establish a Virginia Free File program based on the IRS Free File program by December 31, 2010, effective for the 2010 filing season. This program would be established through a non-monetary agreement between TAX and the "Consortium of Virginia" to offer free, online tax return preparation and filing services to 70 percent of Virginia taxpayers with the lowest incomes. The Virginia Free File Agreement would be based on and subject to the provisions of the agreement between the IRS and the Free File Alliance.

Currently, TAX offers iFile, a free online filing and payment system, which allows most Virginians to file electronically, regardless of income. In 2009, more than 278,000 Virginians filed using iFile. Furthermore, approximately 97 percent of Virginians are eligible to file for free using iFile. TAX would be required to eliminate its current iFile service under this bill.

The effective date of this bill is not specified.

6. **Fiscal Impact Estimates are:** Final. (See Line 8.)

7. **Budget amendment necessary:** Yes.

ITEM(S): 262 and 264, Department of Taxation

8. **Fiscal implications:**

Administrative Impact

It is impossible to determine the administrative impact of this bill. Provided those taxpayers who would be prohibited from filing for free by this bill do not instead file paper returns, this bill would result in an administrative cost savings for the Department of Taxation of \$49,200 in Fiscal Year 2011 and each fiscal year thereafter. To the extent that taxpayers choose to file paper returns instead of paying a member of the Consortium of Virginia to file electronically, TAX's cost to process paper returns would be

approximately \$1 each. Therefore, depending on taxpayer behavior, TAX, may either incur a savings or additional costs.

Revenue Impact

There is no revenue impact for this bill.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

IRS Free File Agreement

The IRS entered into an agreement on October 30, 2002 with the Free File Alliance, a consortium of companies in the electronic tax preparation and filing industry (the "Consortium"). The Agreement was renewed in 2009. The Agreement was established to facilitate the offer of free, online tax return preparation and filing services to low income taxpayers. As part of the Agreement, the Consortium offers free services to taxpayers meeting the qualifications for free offerings. Such offerings, when taken in the aggregate, are currently intended to provide free services to be available to 70 percent or more of taxpayers with the lowest adjusted gross incomes.

For Taxable Year 2009, taxpayers whose adjusted gross income is \$57,000 or less may be eligible to file for free under the federal Free File program, subject to additional restrictions. Taxpayers who do not qualify to file for free under the federal Free File program may still file electronically, but must pay a fee for the service.

The Agreement requires the IRS to provide taxpayers with links to the free services offered by the Consortium through a web page on the IRS's website. In addition, the Federal Free File Agreement has certain restrictions regarding online filing programs that may be offered by the IRS, which prohibit the IRS from competing with the Consortium in providing free, online tax return preparation and filing services to taxpayers.

State Agreements

After the IRS established the Federal Free File Agreement, some states established similar agreements with the Consortium to offer free services to taxpayers, subject to the restrictions in the federal agreement. For 2009, 20 states are listed as having a free file agreement. These states are Alabama, Arkansas, Arizona, Georgia, Idaho, Iowa, Kentucky, Michigan, Minnesota, Mississippi, Missouri, New York, North Carolina, North Dakota, Oklahoma, Oregon, Rhode Island, South Carolina, Vermont, and West Virginia.

Virginia iFile

Currently, TAX provides a free online filing and payment system called iFile. iFile is an application developed by TAX and is available for most Virginians, regardless of income. iFile is not available for some taxpayers that claim certain credits, which excludes approximately 3 percent of Virginians from using iFile. However, iFile is available for taxpayers claiming the earned income tax credit.

In 2009, more than 278,000 Virginians filed electronically using iFile. Based on survey responses, 98 percent of taxpayers who used iFile were satisfied with the service. If Virginia were to implement a service with the \$57,000 threshold that the Free File Alliance currently uses to determine whether a taxpayer is eligible to file for free, over 90,000 Virginians who currently use iFile would no longer be eligible to file for free. This number could be much larger depending on additional eligibility requirements imposed by the Consortium participants.

Of the 278,000 returns TAX received through iFile, 85,000 were submitted by local tax officials. Because most Free File Alliance companies require a taxpayer to file their federal return through that company in order to receive the free electronic filing of the state return, it is likely that the returns submitted by local tax officials would not be eligible to be submitted through the Free File Agreement.

State Comparison

The number of electronically filed returns submitted through state Free File agreements has not been as large as was expected in some states. For example, Massachusetts terminated their Free File Agreement last year in favor of developing their own online filing system for this reason. South Carolina established a Free File Agreement hoping to attract more taxpayers to file electronically, but the Free File Agreement provides approximately the same number of returns electronically as South Carolina's state run online filing program did. Finally, New York receives approximately 100,000 returns electronically under their Free File Agreement. This is less than 36 percent of the amount of electronically filed returns that Virginia receives through iFile.

Proposal

This is a "Section 1" bill that would require TAX to establish a Virginia Free File program based on the IRS Free File program by December 31, 2010, effective for the 2010 filing season. This program would be established through a non-monetary agreement between TAX and the "Consortium of Virginia" to offer free, online tax return preparation and filing services to 70 percent of Virginia taxpayers with the lowest incomes.

This bill would require the Consortium to provide free tax services to certain qualified taxpayers at no cost to the Commonwealth. In exchange, TAX would be required to provide a link through TAX's website to the tax services offered by the Consortium. In addition, TAX would be required to eliminate its current iFile service under this bill.

The Virginia Free File Agreement would be based on and subject to the provisions of the agreement between the IRS and the Free File Alliance. In addition, this bill would require

the Commonwealth to coordinate efforts with the IRS Free File program, the Free File Alliance and the IRS to maximize the awareness of the Virginia Free File program and the claiming of the federal earned income tax credit among eligible Virginians.

The effective date of this bill is not specified.

cc : Secretary of Finance

Date: 2/18/2010 JKM
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