



Franchise Tax Board

Report to the Legislature

April 23, 2009



State of California
Franchise Tax Board

ReadyReturn

Introduction

The Franchise Tax Board (FTB), in accordance with the 2008 budget act, is submitting this report to the Legislature on the ReadyReturn program. The budget specified that we address the following points:

- (a) The cost of the Ready Return program annually since inception by FTB.
- (b) The number of taxpayers participating in the program.
- (c) A summary of other options for taxpayers that do not include the Ready Return model.
- (d) The number of FTB employees working on the Ready Return program.

ReadyReturn Program Background

FTB deployed the ReadyReturn program as a pilot for tax years 2004 and 2005. Following the completion of the pilot, the three-member Board directed staff to offer the program to all eligible taxpayers, beginning with tax year 2007.

ReadyReturn is a voluntary program aimed at easing the tax-filing burden for taxpayers filing simple returns. The premise of ReadyReturn is to use information already available to us to provide taxpayers with their completed return for their consideration.¹ Specifically, we use:

- The name and address information from our account records.
- The filing status, exemptions, and number of dependents from the taxpayer's previous year California individual income tax return.
- The current tax year wage and withholding information that employers report to the Employment Development Department (EDD); which EDD already provides to FTB to assist in processing tax returns.

Each year, we identify taxpayers who are eligible for ReadyReturn based on the above information. For the 2008 tax year, we selected over 1.9 million individuals who had the following information on their 2007 California individual income tax return:

- Single or head of household filing status
- No more than five dependents
- Standard deduction

¹ Taxpayers can review, modify, and file the ReadyReturn or ignore the return and file some other way.

- No credits other than the exemption credits and the renter's credit
- Income only from wages

In addition, selected taxpayers had only one employer in 2008 and total wages no more than \$163,187 for single taxpayers and \$244,785 for head of household filers.²

Taxpayers can check their eligibility for ReadyReturn at FTB's website, by calling a toll-free interactive voice response (IVR) system, or by speaking with an FTB customer service representative. If they are eligible and their return is ready, they have the option to review their ReadyReturn online or request that we send their ReadyReturn to them by mail.

We instruct taxpayers to review their ReadyReturn carefully and make any needed changes. Taxpayers can change all aspects of their return to reflect changes that may have happened since they last filed, such as getting married, having a child, purchasing a house, receiving income from another source, or qualifying for additional credits. Once the return is correct and complete, the taxpayer submits the return to FTB either on paper or via the FTB website.

Participation in ReadyReturn is voluntary: taxpayers have the option of using ReadyReturn or their preferred method of filing a return.

(a) The cost of the ReadyReturn program annually since inception at FTB.

The ReadyReturn program has taken two primary forms since its inception. For the first two years (tax years 2004 and 2005), we conducted ReadyReturn as a pilot program for a limited number of taxpayers. Beginning with tax year 2007, we have offered ReadyReturn to all eligible taxpayers. Due to the differences in these approaches, the cost to administer the program necessarily varies.

Tax Year	Fiscal Year	Cost
2004 (Pilot)	2004/2005	\$222,000
2005 (Pilot)	2005/2006	\$161,000
2006 - Program not offered	-	-
2007	2007/2008	\$482,000*
2008	2008/2009	\$325,000**

* Includes full automation of the program for all eligible taxpayers.

** Included expansion of the program to renters, head of household filers, and dependents.

² The average income of ReadyReturn filers for tax year 2008 was \$30,636, while the median was \$27,434.

Since we do not anticipate further expansions to the program, we anticipate annual costs to be under \$150,000 per year. We can maintain the program at this relatively low cost because we designed ReadyReturn to leverage existing programs. By maintaining the low cost and experiencing increased usage, we expect to produce net savings going forward.

Fiscal Year 2009/10

Cost to Process if Filed on Paper (90,000 x \$2.59)	\$233,100
Cost to Process ReadyReturns (90,000 x \$0.34)	\$30,600
Estimated Cost Savings/Avoidance	\$202,500
Projected ReadyReturn Maintenance Costs	\$125,000
Net Savings to State due to ReadyReturn	\$77,500

Fiscal Year 2010/11

Cost to Process if Filed on Paper (160,000 x \$2.59)	\$414,400
Cost to Process ReadyReturns (160,000 x \$0.34)	\$54,400
Estimated Cost Savings/Avoidance	\$360,000
Projected ReadyReturn Maintenance Costs	\$125,000
Net Savings to State due to ReadyReturn	\$235,000

(b) The number of taxpayers participating in the program.

Tax Year	Eligible Taxpayers	Returns Filed
2004 (Pilot)	51,850	11,620
2005 (Pilot)	50,820	10,582
2006	-	-
2007	732,724	11,253
2008	1,936,741	60,052*
2009**	2,000,000	90,000
2010**	2,000,000	160,000

* Through April 20, 2009.

** Projected.

ReadyReturn Pilot – Tax Years 2004 and 2005

For each of the ReadyReturn pilot years, we selected approximately 50,000 taxpayers for the program. We sent each taxpayer a letter inviting them to participate in ReadyReturn. This mailing provided the taxpayer their completed return, their individual

password to access their return online,³ and instructions on how to participate in the program. We also informed them that they can ignore the invitation. We selected taxpayers who met the general eligibility criteria and had final wage information in our records. To study how the timing of final wage information affects this type of program, we mailed the tax year 2005 letters approximately 30 days later than we did for tax year 2004.

[ReadyReturn Full Implementation – Tax Years 2007 and beyond](#)

Beginning with tax year 2007, we opened ReadyReturn to all eligible taxpayers. To do this, we made several changes to the program. Two fundamental changes affected program participation:

- 1) We no longer sent completed returns to all eligible taxpayers.
- 2) We selected eligible taxpayers at the start of the year and readied the returns as we received final wage data.

For tax year 2007, we primarily relied on various free media opportunities to inform taxpayers about ReadyReturn. We saw an increase in participation when we sent our annual letter describing FTB's online services to ReadyReturn-eligible taxpayers in March 2008. The letter included information on FTB's direct e-file options (ReadyReturn and CalFile), online payment options, as well as other self-service applications on our website. This letter also plays a strategic role in increasing taxpayer engagement in e-services. Due to the effectiveness of this campaign, for tax year 2008 we started the campaign in January.

By conducting our selection process at the start of the year, taxpayers were able to check their eligibility for the program and find out if their ReadyReturn was available. If the ReadyReturn was not yet available, the taxpayer could sign up for an email notification when the return was ready. This engaged taxpayers early in the process, but due to the lag between the time taxpayers get their W-2 and the time we get the final wage information, a large number of taxpayers opted to file using other methods. We see this lag as the biggest challenge to increasing participation.

Another way we are engaging taxpayers with ReadyReturn is through our CalFile program. When a ReadyReturn-eligible taxpayer logs into CalFile, we advise them that their return is available. Taxpayers have the option to continue with CalFile or try the ReadyReturn program. Approximately 20 percent of ReadyReturn filers entered the application through the CalFile offer. Much like the online services letter, we are leveraging existing programs and services to educate taxpayers about ReadyReturn.

³ To use ReadyReturn online, the taxpayer would need to enter their social security number, which we did not print on the invitation.

(c) Other options for taxpayers that do not include the ReadyReturn model.

Taxpayers have a number of options when it comes to choosing how they want to file their California tax return. FTB, various commercial software companies, and professional tax preparers provide these options with varying degrees of support and costs.

Professional tax preparation

Taxpayers may choose from many types of tax preparers, including Certified Public Accountants (CPAs), Enrolled Agents (EAs), tax attorneys, and preparers registered with the California Tax Education Council (CTEC). These preparers may be affiliated with tax preparation franchises, law or accounting firms, financial planning services, or other organizations. The fees these preparers charge vary widely based on the complexity of the taxpayer's return and the level of experience of the tax preparer. FTB offers information about selecting a tax preparer on its website, along with a tool to locate authorized e-file providers in a given area.

To date for tax year 2008, tax professionals have accounted for 70 percent of all individual tax returns filed, or 8.2 million returns.

Non-profit options

We are aware of three non-profit organizations that provide free tax preparation and e-file to eligible taxpayers. The FTB and IRS jointly administer the Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) programs that help individuals with low income and/or over the age of 60 prepare their state and federal income tax returns free of charge.

VITA program helps taxpayers with basic tax returns. The program specializes in assisting disabled taxpayers, those with low to limited income, and non-English speaking taxpayers.

TCE program provides free income tax assistance for middle- or low-income taxpayers, giving special attention to those aged 60 and older.

The Legal Aid Society of Orange County & Community Legal Services of Southeast Los Angeles County provides free income tax preparation assistance to low-income individuals and seniors.

Commercial software options

Website and Boxed Software options

Taxpayers have a number of options if they choose to use commercial software. They can purchase software at a retailer or use the software company's website. The pricing structure for these products varies widely. Generally, these companies charge a separate fee for the federal return and the state return. Some may charge additional fees depending on the complexity of the taxpayer's return, the features of the software the taxpayer chooses to use (for example, a deduction finding tool or importing data from other sources), and the level of post-filing support. When a taxpayer chooses commercial software for e-file, they must send their tax information to the software provider or another third party for processing before FTB receives the tax return. To date, we have received approximately 2 million e-filed tax returns through commercial software, or 17 percent of all individual tax returns.

Free File Alliance

There are free options available for taxpayers who choose to file online. The IRS has a partnership with the Free File Alliance LLC (a group of private sector tax software companies) to provide free federal income tax preparation and e-filing to taxpayers who meet certain qualifications. While all members of the alliance agree to the upper income limit (for tax year 2008 the taxpayer's federal AGI must be \$56,000 or less), each company can set their own eligibility requirements. Individual company offers may be limited to AGI (several top out at \$30,000), age, specific states, and include other criteria. One of the tenets of the Free File program is that the federal government agrees not to provide its own Internet filing product in exchange for vendor-based free offerings.

Many of the companies that offer their software through the IRS Free File also provide state returns, often for an additional charge. The IRS Free File program is prominently featured on the IRS website and provides a tool to help taxpayers determine if they qualify to use Free File and which companies have an offer that meets their needs.

Beginning with tax year 2008, the Free File Alliance offers an alternative to the interview-based filing experience. Through Free File Fillable Forms, the taxpayer selects which forms to complete and enters their information. The form then completes the math and prepares the return for e-file. One of the benefits of this program is that there are no income limits – as long as the forms you need to file are available, you can use the Free File Fillable Forms. A drawback, though, is that taxpayers do not have the option to complete their state return at the same time.

A state-level Free File program has been discussed in many variations since the IRS established its partnership in 2002. Currently, there is no formal state-level Alliance – or body of vendors – coordinating this effort. And, despite efforts by the Federation of

Tax Administrators to facilitate an alliance between Industry and the states that is similar to the federal alliance, there has not been any collective interest by the vendors to do that.⁴ Accordingly, each state that is interested in such a partnership is required to negotiate separate offerings on a vendor-by-vendor basis. Twenty-one states have chosen this approach. In general, the vendors' offerings mirror what they offer through the IRS Free File program (e.g., same income limitations) and require the state to forgo offering its own Internet filing product.

If we eliminated our ReadyReturn and CalFile programs, approximately 130,000 taxpayers (45%) who used ReadyReturn or CalFile in 2009 would not have qualified for the general state-level Free File offerings currently available in other states. This is because their AGI exceeds the AGI upper limits of the Free File offers.

Without ReadyReturn and CalFile, it is quite likely these 130,000 taxpayers may have chosen to paper file because they couldn't e-file for free. If they all paper filed, it would cost us almost an additional \$300,000 in processing costs.

To understand state-level Free File utility in participating states during 2009, we surveyed twenty-one states after the April 15th primary filing season concluded. Seven states had enough information to respond. Among those seven states, approximately 20,000,000 total returns were filed, and 220,000 of them were from their state-level Free File programs. This represents 1% of total returns filed. Comparing that utility rate to California, expected utility could be in the neighborhood of 150,000 Free File returns. This is one-half of what CalFile and ReadyReturn delivered for 2009.

California's Memorandum of Agreement Program

California has offered a state-level "Free File" program since establishing a Memorandum of Agreement program in 1999. Currently five companies participate in this program and provide free e-file for California tax returns. In return, FTB has provided them a page detailing their offer on the FTB website.⁵ Some of the offers are contingent on the purchase of the federal tax return preparation. Others provide completely free state and federal offerings if the taxpayer meets the company's federal Free File qualifications.

FTB does not impose any limitations on what the vendors can offer through this program; each vendor is free to customize their offering as they see fit. As a result, the offerings can be quite varied from vendor to vendor. The table on page 9 shows the vendors and their offerings for tax year 2008.

⁴ The federal Free File Alliance model was never originally intended by the software providers to extend to the states, which is a central reason why there is not full integration of free federal and state offerings.

⁵ In 2009, these pages received over 65,000 visits. The vendors are not required to disclose the number of free returns they provided through their offering.

Participants in California's Memorandum of Agreement Program Tax Year 2008	
Vendor	Free State Return If:
E-File-Tax>Returns.org	Pay \$29.95 for federal tax return
ezTaxReturn.com	Pay \$29.95 for federal tax return
FileYourTaxes.com	<ul style="list-style-type: none"> • Form 540 2EZ • Income limits <ul style="list-style-type: none"> ○ \$25,000 – married or head of household ○ \$10,000 – single • No income limit if under 18
Legal Aid Society of Orange County	<ul style="list-style-type: none"> • Federal AGI of \$30,000 or less OR • Qualify for the federal Earned Income Tax Credit (EITC)
TaxSlayer.com	Household income less than \$56,000 and meet any of the following requirements: <ul style="list-style-type: none"> • 25 years of age or younger • 68 years of age or older • Federal AGI of \$10,000 or less, regardless of age • Qualify for the Earned Income Credit (EIC) • Active Duty Military ⁶

[FTB-provided filing options](#)

Paper Tax Forms

FTB provides official tax forms and instructions to taxpayers by mail, at public distribution sites (such as post offices and libraries), and on our website. Taxpayers can print the tax forms they need from our website and complete them by hand or fill them out online and print them to file by mail.

CalFile

Since tax year 2002, FTB has provided CalFile. This free online e-file service uses a question-and-answer format to guide taxpayers through completing a Form 540. CalFile uses the taxpayer's responses to determine eligibility for certain credits and calculate the amount of the credits and deductions. Taxpayers get a complete copy of their return before deciding if they want to e-file it. If they choose to e-file their CalFile return, they submit it directly from our website into our e-file processing system. Since tax year 2007, CalFile has been available in both English and Spanish.

Over 6.4 million taxpayers qualify to use CalFile each year. The general qualifications for CalFile are:

- Full-year California resident filing a current year tax return

⁶ Includes Reservists, National Guard and Coast Guard.

- Income less than the following amount – based on filing status:
 - \$163,187 for single and married/registered domestic partnership (RDP) filing separately taxpayers
 - \$244,785 for head of household taxpayers
 - \$326,379 for married/RDP filing jointly and qualifying widow(er) taxpayers
- No more than 10 dependents

Detailed qualifications are available online at www.ftb.ca.gov/online/calfile/qualifications.shtml.

Taxpayers have come to depend on CalFile for a completely free state e-file experience. For tax year 2007, more than one-third of taxpayers who chose CalFile had used CalFile the year before. CalFile experienced 56 percent growth over the last three tax years, from 141,833 tax returns for tax year 2006 to 223,294 to date for tax year 2008. When we combine the CalFile volume with the number of returns filed through ReadyReturn the growth rate exceeds 98 percent.

CalFile has the second largest market share among do-it-yourself e-file products. Through April 15, 2009, nearly 10 percent of do-it-yourself e-filers have chosen CalFile. Taxpayer use of CalFile is growing faster than the rest of the market.

Calculating Form 540 2EZ

Beginning with tax year 2007, FTB provides a calculating Form 540 2EZ. This form performs simple math calculations and looks up the tax amount based on the taxpayer's entries. The taxpayer then prints and mails the form to FTB. This form was downloaded approximately 190,000 times in each of the two years FTB has offered the program.

(d) **The number of FTB employees working on the ReadyReturn program.**

Thirty-six FTB employees participated in the effort to make ReadyReturn available to all eligible taxpayers. These employees spent as little as 10 hours over the six months of development while some were dedicated to the project at 80 percent for that period. The total one-time cost was 5.7 personnel years. These employees contributed by writing and validating requirements, coding applications, testing the programs, integrating the various systems that make up the ReadyReturn program, and developing support procedures.

The annual maintenance cycle generally runs from September through January. For those five months, approximately the same number of employees spent between one and twenty percent of their time supporting the program. The total expenditure was 1.9 personnel years. We project this will decrease to 1.5 personnel years going forward.