

REPEALING THE HIDDEN TAX

A TULSA NONPROFIT HELPS WORKING POOR FAMILIES
AVOID EXPENSIVE TAX PREPARERS, MAXIMIZE REFUNDS,
AND BEGIN SAVING FOR THE FUTURE

BY DICK MENDEL

As April 15 crept nearer in 1996, Angela Taylor did like tens of millions of low-income working parents: She dragged herself to a local tax preparer's office.

In prior years, Taylor had let her mother fill out her tax forms. But then Taylor, a single mother in Tulsa, Oklahoma, began to worry. "My mom wasn't a certified preparer," she explains, "and I just felt better" having the returns done professionally. Taylor was also lured by the preparer's advertisements promising to deliver the refund checks within two days of filing a return.

Angela Taylor, pictured with her daughters Cydnee, 9, and Erielle, 5, has been using CAP's tax preparation program since 1997. In 1996, she paid more than \$100 to a commercial tax preparer.

She made an appointment with Mr. Tax, Inc., and then sat by as the firm filled out her tax forms, filed them electronically, and completed the paperwork for a rapid refund loan. Taylor also signed a form granting Mr. Tax a thick slice off the top of her refund.

Today, Taylor cannot recall precisely how much she paid the tax preparer—at least \$100, she says—but she does remember what she got for her money.

"[The refund] was supposed to take 48 hours," she says, "but they gave us just a little bit after two days, and we waited at least two weeks for the rest. I was very frustrated. I said I wouldn't go back, and I never did go back."

Had she lived anywhere except Tulsa, Taylor would have been hard-pressed to keep that pledge. Increasingly, the federal tax code for low-income

families—while offering a wealth of possible benefits—requires filers to navigate a swamp of complicated forms, instructions, and worksheets. Free tax assistance for low-income filers is scarce throughout most of the nation.

But not in Tulsa. There, a local nonprofit agency has developed perhaps the most ambitious program in the nation to provide free tax help to low-income workers. Operated by the Community Action Project of Tulsa County (CAP), the program has prepared returns for more than 12,000 wage earners in each of the last two years, helping these Tulsa taxpayers avoid roughly \$2 million in preparer fees over the two years and reap \$27 million in federal and state tax refunds.

Angela Taylor got wind of the program early in 1997 and made an appointment. The service was quick, convenient, and free. Better yet, the forms were completed on computer and filed electronically, allowing Taylor to collect her refund in less than three weeks—almost as fast as Mr. Tax. She's been a loyal customer ever since.

THE HIDDEN TAX

Think of it as a hidden tax on the working poor—\$75, \$100, sometimes even \$200 per year plucked from the pockets of America's most vulnerable families as they struggle to earn their way out of poverty.

As welfare reform pushed millions of formerly dependent families to sink or swim in the job market in the 1990s, the federal government significantly

Low-income taxpayers filing for the Earned Income Tax Credit paid commercial tax preparers at least \$633 million last year to complete their tax forms. Including electronic filing fees and rapid refund costs, these working poor filers almost certainly spent more than \$1 billion in 2001 for tax services.

ITEMIZING THE HIDDEN TAX

How Much Do Tax Preparers Charge Low-Income Families?*

Tax Return		
Form 1040	\$	40.00
W-2 Forms		10.00
EITC		15.00
Basic Cost for Preparing Return		\$ 65.00
Electronic Filing		
IRS Form 8453 (required for electronic filing)	\$	15.00
Tax Return Plus Electronic Filing		\$ 80.00
Refund Anticipation Loan		
RAL Preparation Fee	\$	15.00
Cost of Bank Loan		64.95
Total Cost		\$159.95
(Tax return plus electronic filing plus refund anticipation loan.)		

*Prices taken from Taxes1.com, an internet-based tax preparer, for a low-income taxpayer who has income from two employers, is eligible for EITC, and is entitled to a tax refund of \$1,000 to \$1,500.

expanded the Earned Income Tax Credit (EITC) to reward low-income families who work and to help them make ends meet. For tax year 2001, the credit was worth up to \$4,008 for working families with two or more children, not including the additional earned-income credits enacted by several states in recent years.

These benefits come with a hitch, however. The Internal Revenue Service publication explaining the EITC is 54 pages long, including six separate worksheets. As Michael Mares of the American Institute of Certified Public Accountants told a congressional committee, "It is unreasonable to expect those individuals entitled to the credit (who will almost certainly NOT be expert in tax matters) to deal with this complexity."

As a result, a large and growing share of the credit is being paid to tax preparers who fill out tax returns for low-wage workers. Although the finances of low- and moderate-income families tend to be far simpler than those of more affluent families, a recent IRS study showed that 60 percent of families filing for earned-income credits in 1997 used paid tax preparers, compared with 51.8 percent of all filers nationwide.

In addition to charging low-income clients to complete state and federal tax returns, many preparers have also aggressively marketed refund anticipation loans (RALs) that allow cash-strapped families to collect their refunds within 48 hours. Preparers typically charge \$75 to \$100 in fees and interest for RALs. Given that the IRS provides refunds within two to three weeks for taxpayers who file returns electronically, that can

translate into an effective annual interest rate on RALs of more than 100 percent.

John Wancheck of the Center on Budget and Policy Priorities, a Washington, D.C., think tank, estimates that taxpayers filing for the earned-income credit paid at least \$633 million in 2001 for tax preparation charges alone. When electronic filing fees and rapid refund costs are included, EITC filers almost certainly spent more than \$1 billion last year for tax services.

“Paying for tax preparation takes money away from [EITC] benefits,” the center declared in its *2001 Earned Income Credit Outreach Kit*. “It means that workers have less money to help pay bills and care for themselves and their children. This runs counter to a primary goal of the earned-income credit: improving people’s financial stability.”

HELP—BUT NOT ENOUGH—FROM THE IRS

The IRS has long recognized that its complex rules are beyond the comprehension of many taxpayers. Since 1977, the agency has been sponsoring free tax preparation through the Volunteer Income Tax Assistance (VITA) program. VITA operates in more than 8,500 sites nationwide, providing information to 1.8 million taxpayers each year.

Unfortunately, VITA programs do not serve the vast majority of low-income working families. The IRS provides no direct funding for local VITA projects to hire supervisors or coordinators, not even to support the recruitment of volunteers. Many VITA sites do not complete returns for workers with income from self-employment—roughly 17 percent of EITC recipients. And many VITA sites are located in suburban areas far from the homes of potential earned-income credit recipients. The IRS offers free training to VITA volunteers nationwide, along with forms, computers, and tax software. But its training curriculum lumps the EITC and its complex rules together with six other credits into a single two-hour session.

In June 2000, an internal IRS study found that VITA sites completed returns for nearly 500,000 taxpayers in

1997, of whom 101,000 were low-income workers claiming the EITC. Ron Smith, chief of community partnerships for the IRS, insists that these figures undercount VITA’s production. But even if VITA sites completed twice that number of EITC returns—200,000—it would still represent only 1 percent of the 19.5 million families nationwide who claim the EITC each year.

In recent years, the IRS has begun to supplement VITA by opening “walk-in” offices throughout the nation. These offices, which are staffed by IRS employees from January through mid-April, prepared 850,000 tax returns in 2000, but the IRS does not keep data on how many of these returns were filed by low-income workers and EITC claimants. Smith says that the IRS has also shifted its strategy in the past year to focus on partnerships with community organizations like CAP, rather than stand-alone VITA programs.

But many advocates argue that the IRS should provide direct funding to local programs that offer free tax assistance. “Given the significance of the earned-income credit . . . and the enormous number of eligible families,” says Wancheck of the Center on Budget and Policy Priorities, “there needs to be a source of federal funds to make sure that people get the full effect of these tax credit programs, rather than subsidizing and enriching the tax preparation industry.”

TAKING A CHIP OFF THE H&R BLOCK

While most low-income taxpayers nationwide remain caught between a rock (paying for tax preparation) and a hard place (navigating the EITC forms on their own or forsaking the credit), in Tulsa a free, full-service tax preparation service has emerged over the last seven years to fill the void.

The program is the brainchild of Steven Dow, a Yale-trained lawyer and former investment banker who followed his wife to Tulsa in 1990. Two years later Dow took the reigns of a local nonprofit agency called Project Get Together. The agency—which changed its name to Community Action Project of Tulsa County in 1998—has been growing ever since, becoming the recipient of Tulsa County’s

\$650,000 per year Community Service Block Grant and taking over the county's Head Start program.

In 1994, Dow initiated a campaign to inform Tulsa's low-income residents about the federal Earned Income Tax Credit. First enacted in 1975, the credit had been expanded under Presidents Reagan (in 1986), Bush (in 1990), and Clinton (in 1993). Yet many eligible families still didn't know about the credit in the early 1990s and weren't taking advantage.

The outreach campaign made thousands of Tulsans aware of the EITC. But when residents asked where they should get their taxes done, Dow's agency could only refer them to local VITA programs. "When

people tried to look around, they found that the VITA program wasn't operating in the neighborhoods where they lived, or in the hours they weren't working," says Dow. "We found that a large number of our clients were taking the information that we gave them and weren't able to make use of it ... or they were paying a lot of money to commercial preparers to get their taxes done."

"It begged the question of are we going to step up to the plate and do something about the problem," Dow recalls. "That's when we looked and said, hey, maybe we need to look at ourselves becoming a free tax assistance site."

A BUDDING TAX

Seven hundred miles from Tulsa, Chicago's Center for Law and Human Services began offering free tax preparation for low-income workers in 1994. The center's Tax Counseling Project has been growing ever since, and growth has been especially rapid since 1999 when Mayor Richard M. Daley launched a citywide campaign to increase public awareness of EITC benefits.

Daley grew interested after seeing research showing that some 60,000 Chicago workers eligible for earned-income credits were not claiming the benefits, depriving the city of \$90 million in potential revenues each year. "This is money that's there for the asking," Daley told a group of business leaders in December 1999. "It would be spent in Chicago. It's not welfare. This is for people who work for low pay instead of going on welfare."

The mayor's office has created a public-private partnership with foundations, business organizations, and community agencies, and it has spearheaded an all-out publicity blitz. In 1999-2000, the campaign included: 4.2 million notices sent out with utility bills; one million other flyers; hundreds of radio advertisements; and messages on tens of millions of transit cards, movie trailers, and grocery bags. The Illinois Department of Human Services has also supported the effort, mailing information letters to almost one million families each of the past three January's.

Thanks to this outreach, the Tax Counseling Project served 10,450 clients in 2001—a 45 percent increase since 1999. Likewise, another Chicago-based tax project, Tax Assistance Program—It Adds Up, grew from 2,581 tax clients in 1999 to 4,354 in 2001—a 68 percent increase. Together, the two agencies helped low-income taxpayers qualify for more than \$16 million in tax refunds last year.

SETTING UP SHOP

During the second half of 1994, Dow raised funding from the city's Community Development Block Grant and deputized Dick Jackson, an energetic volunteer who had recently retired from the aerospace industry, to take charge of program development. "There was not a whole lot of what I would call careful planning that first year," Jackson says. "It was kind of sink or swim."

Jackson determined that computers would offer the most efficient and reliable method for completing tax returns. Computer tax computation would also allow the program to file returns electronically, enabling clients to receive their refunds within two or three

weeks rather than the four to eight weeks that paper filers typically wait. Jackson also pulled together a training curriculum to teach volunteers about IRS and EITC rules, and to orient them to the computers and software they would use to complete the returns.

In February 1995, the fledgling tax project commandeered a classroom and opened for business. "We had no idea what to expect," Dow recalls. "We did it to see whether or not in fact there was a market demand and need for it." The response was overwhelming. "The first couple of days were just pandemonium," says Jackson. "We just couldn't keep up with the demand."

PREP MOVEMENT

Tax preparation initiatives are also active in other jurisdictions. The AccountAbility Minnesota project in Minneapolis–St. Paul prepared 6,500 returns for low-income families in 2001, while Detroit's Accounting Aid Society prepared 5,000 returns. In San Francisco, Tax-Aid, a local nonprofit agency, prepared 1,195 returns in 2001 and generated \$965,000 in tax refunds.

The Annie E. Casey Foundation has identified free tax preparation as a promising economic empowerment strategy for its *Making Connections* project—a 22-city initiative to strengthen families and uplift troubled neighborhoods. In Camden, New Jersey, for instance, local leaders responded to a September 2000 briefing about tax preparation by recruiting and training 36 volunteers and opening 20 new VITA tax preparation sites. Milwaukee's *Making Connections* team also initiated a tax project in 2001, and at least four other *Making Connections* cities are planning tax preparation initiatives in 2002 as part of their efforts to promote saving among low-income families.

"[Tax preparation] is really starting to see movement among people who are concerned about how to help people move themselves out of poverty," says Deborah Blank, executive director of the Social Development Commission, which is coordinating Milwaukee's new citywide EITC tax preparation campaign in partnership with Mayor John Norquist. "Historically we've been focused on jobs, and jobs are very important. But now we recognize that how people use the money they have is equally important. How do you help them save some of that money?" Increasingly, experts are recognizing that tax preparation services are part of the answer.

The program served 1,201 taxpayers in that first year, and generated more than \$1.3 million in tax credits and refunds. The following year CAP served more than 3,000 clients and generated close to \$4 million in credits and refunds. Apart from a slight downturn in 2001, the program has continued to grow ever since—climbing above 12,000 clients and \$12 million per year in credits and refunds in 2000 and 2001.

“Each year,” Dow says, “we’ve looked at what kinds of refinements we need to make to make the program better and more responsive.”

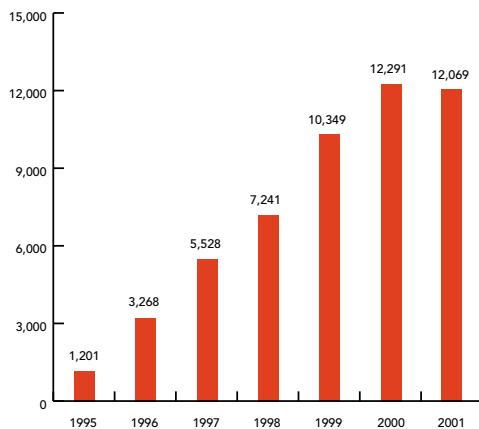
In 1996, Dow hired communications consultant Pat Kroblin to develop a sophisticated public relations strategy for the tax program. Kroblin forged a partnership with KTUL-TV, the local ABC television affiliate, which has produced advertisements about the program each year since 1997 and airs

more than 300 every tax season. This partnership is one aspect of a multifaceted annual marketing campaign that includes more than 12,000 postcards to former customers, plus billboards; posters; flyers; paid advertisements on commercial radio; placards on public buses; and newsletter features distributed by the power company, the United Way, the Tulsa housing authority, and others.

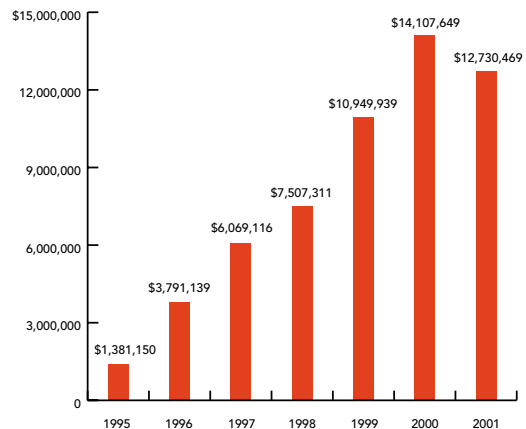
Also in 1996, Dow persuaded the Bank of Oklahoma to host the program. For the last seven years, each February to April, the bank’s branch at Lewis Avenue and Pine Street has turned into a bustling tax preparation office. In 2000, almost 6,000 taxpayers completed their returns at this site. (CAP also operated five other tax sites in 2001—its own headquarters, a credit union, a Latino church, and two suburban sites operated in partnership with the American Association of Retired Persons.)

TAX PREPARATION TAKES OFF IN TULSA

Tax Returns Prepared



Refunds Generated for CAP Tax Clients



Source: Community Action Project of Tulsa County.

Angela's IDA

In 1998, after having her taxes prepared by the Community Action Project of Tulsa County and collecting a large refund, Angela Taylor placed some of her refund into an Individual Development Account (or IDA). For every dollar Taylor saved, CAP promised to contribute a dollar to the account—two dollars if she used the money to buy or improve a first home. Taylor could also use the account to invest in college, a small business, or a retirement account.

In three of her four years in the program, Taylor saved the maximum of \$750. Early on, she used the money to pay for new floors and a new air conditioning system for her home in the Owen Park neighborhood—improvements she could never have afforded on her modest earnings as a social worker. In 2000, Taylor opened an individual retirement account and contributed the \$2,000 maximum.

In addition to these tangible rewards, Taylor says that CAP's IDA program has gradually shifted her thinking about money and work.

"Before, I would work a while and quit, work a while and quit. But now I'm really thinking about the future," she explains. Taylor is especially proud of the contribution she made to her retirement account. "I would never have done that before," she says. Her determination to start saving for retirement began when she looked at a printout in a CAP finance seminar, "It showed that if I contribute \$2,000 a year I'll have \$400,000 by the time I retire, and that sounds real good," Taylor recalls. "My continuing goal is to find some way to put in that \$2,000 every year and see if that \$400,000 really works."

Taylor also points to the effects of the IDA program on her family. All three of Taylor's children (ages 5, 9, and 13) have opened savings accounts with a local credit union, receiving a free gift every time they make a deposit. Taylor's middle child, Cydnee, saved more than \$180 by depositing her allowance, Taylor says, "rather than buying chips and candy and stuff."

"I'm showing my kids how to save, even when your income is low. I'm showing them that they can set goals and reach them."

Individual Development Account (IDA): A dedicated savings account designed to help low-income families build assets and save for the future. IDA programs have emerged in more than 250 communities nationwide since 1991 with support from government agencies and private foundations. They offer a financial match for each dollar saved by participants for long-term investments in home-ownership, home improvement, post-secondary education (or vocational training), entrepreneurial business, or retirement. In addition, IDA participants receive financial literacy training to clean up their credit, establish a budget and savings schedule, and manage their money over the long term.

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—John Wancheck, CENTER ON BUDGET AND POLICY PRIORITIES

Last year, the Bank of Oklahoma made a new service available for CAP tax clients who do not have bank accounts. The bank provided coupons to cash tax refund checks for just \$2 each—helping families avoid commercial check-cashing operations that typically charge \$45 to \$75 (3 to 5 percent) to cash a \$1,500 tax refund check.

In 1999, Dow convinced the Corporation for National Service to send a team of 14 AmeriCorps volunteers. The following year, AmeriCorps sent two teams to take part in the tax program, and it sent one team again in 2001. Because volunteers could devote themselves to the project full time, the AmeriCorps teams proved invaluable. “Without them,” Dow says, “we wouldn’t have been able to serve nearly as many folks as we have.”

In 2001, CAP added a new tax service focused on immigrants, particularly Tulsa County’s rapidly growing Latino population, which tripled between 1990 and 2000 from 11,000 to 33,000. Many of the immigrants entered the country illegally and lack

valid social security numbers, making them ineligible for the EITC. Nonetheless, many need tax assistance urgently. Many illegal workers give employers fake social security numbers and have substantial taxes deducted from their paychecks. Few are aware that by obtaining a valid tax identification number from the IRS, they can begin to file tax returns legally and collect tax refunds. Having a tax number and filing tax returns can be crucial steps on the path to securing permanent residency status in the United States.

In the first six months of 2001, CAP’s Intercultural Tax Service project requested tax identification numbers for 1,232 area residents and completed 511 tax returns, helping immigrants secure a total of more than \$450,000 in tax refunds.

PLANTING A SEED FOR SAVINGS

In 1997, CAP launched a parallel effort to help tax clinic clients and other low-income families turn their tax refunds into nest eggs for the future.

Employing an increasingly popular strategy known as Individual Development Accounts (or IDAs), CAP recruits interested low-income families (earning less than \$25,000 for a family of four), enrolls them in a series of seminars on personal finance, and asks them to contribute at least \$10 per month to their IDAs—up to a maximum of \$750 per year. Using funds from foundations and government agencies, CAP contributes a dollar to each account for every dollar participants save to pay for education or retirement, or to start or expand a small business. CAP adds \$2 to each account for every dollar saved to buy or repair a first home.

Thus far, CAP has recruited 617 participants into its IDA program, and these participants have saved \$450,000 and received \$590,000 in matching contributions. Most participants—like Angela Taylor—were recruited into the IDA program after having their taxes prepared. And, like Taylor, most praise not only the financial support provided through the IDAs but also the psychological shift they experienced as they began to save for the future. (See “Angela’s IDA,” page 35.)

Jeri Curtner, a mother of three, says that participating in the program was a crucial step in rebuilding her life after a difficult marriage and divorce. “You get a super sense of self-worth and well-being when you start saving. . . . When you see yourself doing something that’s going to amount to something, going to grow, then you have some hope.”

LOOKING FORWARD

Recently, Steven Dow has been stepping back and considering the future. In the short run, he must find a way to replace the AmeriCorps volunteers who have been a crucial part of his team to date. After sending volunteer teams three years in a row, the Corporation

for National Service—which oversees AmeriCorps—has informed Dow that it will be sending no more.

Dow is also searching for additional funds to pay for clerical and phone support to reconnect the project’s dedicated phone line. Last year, budget shortfalls led Dow to cancel the telephone service, leaving tax clients unable to schedule their appointments ahead of time for the first time in years. The change caused many clients to complain, and it contributed to the slight drop-off in participation in 2001.

For the long term, Dow is thinking less about how to expand the tax program than about how he might one day dismantle it. “The mission of this agency is to build genuine self-sufficiency for our clientele and to recognize that once prepared and equipped and tooled and trained, they can accomplish a heck of a lot,” he says. “In an ideal world there wouldn’t be a role [in tax preparation] for an agency like ours. There are plenty of other issues that we can be worrying about.”

Unfortunately, Dow concedes, the day when he’ll be able to close down the program has not yet appeared on the horizon.

“As long as there’s a commercial preparer out there that’s going to gouge our clients and charge predatory pricing and entice them to do rapid loans, and [as long as there are] check cashers charging them 3 or 4 or 5 percent of the amount of their refund to cash their refund check. . . . As long as that exists as the market alternative, then yeah, we’re going to provide a much cheaper and better alternative [rather] than let that product predominate.”

Dick Mendel is the editor of ADVOCASEY.