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TAX REPORTBy TOM
HERMAN

Ethics Rule May Help Taxpayers Learn if Firms Outsource Returns

June 29, 2005

As concerns mount about the growing outsourcing trend of sending tax returns to preparers in other countries, a new ethics ruling for accountants could help many Americans figure out if their tax preparer engages in the practice.

An American Institute of Certified Public Accountants ethics ruling, effective Friday, will require institute members to alert clients whose returns are being outsourced. An official of the institute, which has about 350,000 members, says the ruling requires an AICPA member to inform the taxpayer, "preferably in writing," that the accountant may be using a "third-party service provider" when providing professional services.

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This warning must be done prior to sharing any confidential client information, such as tax-return data, with the outside firm. Failure to comply could lead to disciplinary action, an official says.

Tax-return outsourcing has become a delicate issue amid growing concern about taxpayer-privacy protections, identity theft and other issues. Accountants say the number of returns being outsourced, especially to India, has increased rapidly in the past few years, although the number represents a tiny fraction of the 133 million or so individual income-tax returns filed with the Internal Revenue Service.

Industry analysts say outsourcing offers many advantages, including significant cost savings, speedy turnaround and readily available workers at tax season.

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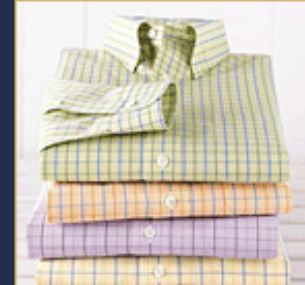
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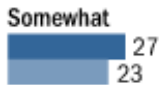
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Tax Facts

GETTING HELP: Many taxpayers agree it's important for the IRS to have office locations they can visit and get answers to questions.



The latest survey, done in July 2004, was based on about 1,000 interviews. The numbers don't add up to 100% since not everyone responded

Source: IRS Oversight Board taxpayer attitude survey

Some major accounting firms say they don't do any outsourcing, while others who do some outsourcing say they already notify clients who may be affected. For example, KPMG LLP has "previously notified and obtained the permission of any clients whose tax returns are now being outsourced," says George Ledwith, a KPMG spokesman. While the "vast majority" of tax returns are processed in this country, KPMG is processing "some" individual tax returns outside the U.S., he says. "We expect that number of returns to increase modestly over the next

few years."

H&R Block Inc., the nation's biggest tax-preparation company by individual returns prepared, "does not outsource tax preparation," says Tom Linafelt, a spokesman.

The AICPA ruling is effective for all professional services performed on or after July 1, except for services done under agreements in existence on June 30 that are completed by year end.

One big concern many taxpayers may have about outsourcing is who would be responsible in case an outside firm makes a costly mistake. The AICPA said another ethics ruling emphasizes the institute's "long-standing belief" that members who outsource returns "remain responsible for the work performed" by that outside firm. The institute also is taking steps designed to protect tax-return confidentiality.

The institute ruling doesn't specify the wording an accountant must use. Since it is easy to overlook boilerplate language, anyone leery of having their confidential tax-return data zapped around the world should take the time to ask the preparer to specify in writing whether the return's preparation is being outsourced. If the answer is yes, press hard for details.

The IRS approves a tax break for buyers of a Toyota hybrid vehicle.

The IRS has added the model year 2006 Toyota Highlander Hybrid to the list of vehicles eligible for the "clean-burning fuel deduction." Thus, someone who buys one of the approved hybrid gas-electric vehicles new this year may take a tax deduction for 2005 of as much as \$2,000. The buyer must be the original owner. This one-time deduction is taken for the year the vehicle first is used.

Buyers don't have to itemize their deductions to claim this break.

Limited Time Values end Wednesday, June 29, 2005.

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Lawmakers revive efforts to protect telecommuters.

Rep. Christopher Shays, a Connecticut Republican, and Sen. Christopher Dodd, a Connecticut Democrat, are trying to win approval for the Telecommuter Tax Fairness Act of 2005. The bill comes in the wake of high-profile court victories won by New York in cases affecting telecommuters who worked for New York employers and lived in other states. For example, New York State's highest court ruled this year that Thomas Huckaby, a computer specialist in Nashville, Tenn., had to pay New York tax on all his income from a New York employer -- even though Mr. Huckaby spent only 25% of his time there.

The Shays-Dodd bill would block a state from imposing nonresident income taxes on the salary of a nonresident for any period of time when that nonresident was physically present in another state, says Nicole Belson Goluboff, a Scarsdale, N.Y., lawyer specializing in legal aspects of telework.

* * *

IRS plans to close 68 taxpayer-assistance centers attract growing fire.

Among the strongest critics is Montana Sen. Max Baucus, the ranking Democrat on the Senate Finance Committee. He is part of a coalition of senators trying to block the IRS's planned taxpayer-service cuts, which include shutting the 68 centers later this year. The 25 senators recently sent a letter on the subject to the chairman and the ranking member of a Senate Appropriations subcommittee.

"It is incumbent" upon the federal government to provide "quality, accessible assistance" to every taxpayer trying honestly to comply, the senators said.

* * *

BRIEFS: Tax fraud committed by prison inmates will be the subject of a hearing today of a House Ways and Means subcommittee headed by Rep. Jim Ramstad (R., Minn.).... President Bush's advisory panel on federal tax reform is expected to hold another public meeting next month. Its report is due by Sept. 30.

Write to Tom Herman at taxreport@wsj.com

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