

Legislative Recommendation #5**Require the IRS to Work With Tax Software Companies to Incorporate Scanning Technology for Individual Income Tax Returns Prepared Electronically But Filed on Paper****PRESENT LAW**

Present law does not address the treatment of individual income tax returns prepared electronically but mailed and filed on paper.

REASONS FOR CHANGE

In recent years, about 90 percent of individual income tax returns have been submitted electronically. While this percentage is relatively high, about 14 million returns are still submitted on paper.¹ When the IRS cannot capture the data from a tax return electronically, IRS employees must enter the data from paper-filed returns manually. The manual transcription of millions of lines of return data is expensive, produces transcription errors, and delays return processing and the payment of tax refunds.

Technology is available that would allow the IRS to scan paper returns prepared with tax return preparation software and capture the data efficiently. To enable the IRS to utilize one form of scanning technology, known as “2-D barcoding,” tax return preparation software would generate and imprint a horizontal or vertical barcode containing all return information on the return. The IRS, upon receiving the paper return, would scan the barcode, capture the data, decode it, and process the return as if it had been transmitted electronically. Many states have been using 2-D barcoding for paper-based income tax returns for more than a decade. The IRS itself has partnered with the software industry to enable Schedules K-1 to be filed with a 2-D bar code. In addition, the IRS has adopted another type of scanning technology, known as “optical character recognition,” to process certain forms filed on paper. With this technology, the IRS scans the paper-filed return (without a barcode), captures the data, stores the tax form images and data in an electronic format, and processes the return as if it had been e-filed.²

While scanning technology is not considered e-file and still involves the submission of a paper return, it produces significant advantages over traditional paper filing, including (i) faster processing of tax returns and therefore delivery of refunds, (ii) more accurate recording of tax return information, and (iii) cost savings due to the reduction in training, recruiting, and staffing for manual data transcription. Despite these benefits, the IRS has not availed itself of scanning technology (*e.g.*, 2-D barcoding, optical character recognition, or similar scanning technology) for individual income tax returns. The IRS can improve the accuracy and efficiency of its return processing by working with tax preparation software companies to ensure that individual income tax returns prepared with software but filed on paper can be scanned.

1 IRS, Filing Season Statistics for Week Ending October 16, 2020, <https://www.irs.gov/newsroom/filing-season-statistics-for-week-ending-october-16-2020> (last visited Nov. 23, 2020) (showing 165,624,000 total returns and 151,812,000 e-filed returns).

2 See Internal Revenue Manual (IRM) 3.41.274, General Instructions for Processing via SCRIPS (Nov. 5, 2019); IRM 3.41.275.1, Program Scope and Objectives (Nov. 14, 2017).

RECOMMENDATION

- Direct the IRS to work with tax preparation software companies to place 2-D barcodes or similar machine-readable codes on individual income tax returns prepared electronically but filed on paper.³

³ For legislative language that would impose a requirement for 2-D barcode, or scannable code, technology, see Taxpayer First Act of 2018, S. 3246, 115th Cong. § 2104 (2018).