From the Editor:

An Easier or More Costly Tax Day With I-File?

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Tax day came and went last week, and as people rushed to their accountants with shoeboxes full of receipts or sat down in front of the computer to file their returns online, a report from a free-market advocacy group said that a proposed IRS electronic filing portal flunks a cost-benefit analysis.

The report from the Computer and Communications Industry Association said the proposed I-File program would cost about $132 million more than it would save over 10 years and wouldn't increase the number of electronic filers. Noting the Service's troubled technology record, the report recommends that e-filing be left to the private sector (p. 248).

But the current system isn't producing the way it's supposed to. Congress had set a goal of 80 percent of returns to be filed electronically by 2007, but last year only 58 percent of returns were filed that way. National Taxpayer Advocate Nina Olson called the report biased and said that there are many self-preparers out there who would like to e-file but don't want to pay for the privilege. Olson admitted that she was one of the 43 million taxpayers who last year purchased return preparation software to calculate their taxes but printed the forms and mailed them to the IRS. ''I will not pay $14.95 to file my return with the government,'' she said.

Call me cheap, but I won't pay a dime to file my return either. I still file with the IRS on paper, but I would e-file directly if I could. I file my local return in the District of Columbia, which has a great filing portal that is free and doesn't require software or a third-party preparer. Completing and filing my D.C. return took 12 minutes this year. Admittedly, the District piggybacks on the federal return, making the process faster and easier than a federal system would be, but if D.C. and some of the states can set up a good portal, so can the IRS. I can't believe that Olson and I would be the only ones to use it.

In news analysis, Joann Weiner has some thoughts about filing returns and the burden on taxpayers, particularly low-income taxpayers. She also highlights some proposals to simplify the tax system, such as proposals to take millions of taxpayers off the rolls or adopt prepopulated returns, like California's ReadyReturn (p. 249).

Some of these proposals were discussed at a Senate Finance Committee hearing on tax reform, which included discussion of whether the United States should adopt a consumption tax (p. 228). However, some think the time isn't right for such a change (p. 313).

Presidential Politics and Returns

Millions of average folks weren't the only ones filing their returns as the April 15 deadline approached. Last week, Sen. Barack Obama released his 2007 return, paying about $1.4 million in taxes on $4.2 million of income (p. 240).

Sen. John McCain also released his 2006 and 2007 returns last week, paying about $84,000 in taxes on $259,000 of income for 2007. McCain and his wife, Cindy, file separate federal returns, and Cindy will not release her returns. But the couple has released statements that show how they allocate their income for state tax purposes in Arizona. The McCain returns and statements, as well as the returns of Obama and Sen. Hillary Rodham Clinton are available at http://www.taxhistory.org.

If McCain is residing at 1600 Pennsylvania Avenue next year, we might see a very different type of tax code, one with an optional alternative tax system. Sketching out his plan in a speech in Pittsburgh, McCain said taxpayers could choose to use the current system or elect a simplified system with two tax rates and a standard deduction. The presumptive Republican nominee's plan would also repeal the alternative minimum tax, cut the corporate tax, end earmarks, and cut spending. McCain also suggested a gas tax holiday that would temporarily eliminate the federal gas tax from Memorial Day to Labor Day. Democrats in Congress immediately criticized the idea, saying it would endanger transportation infrastructure (p. 235).

Conjuring the idea of a McCain administration come January 21, 2009, Marty Sullivan has written a ''confidential memorandum'' to the new administration providing some revenue estimates for the new president based on last week's campaign position paper on his economic plan. Sullivan tells McCain that his tax proposals do not compute (p. 236).

Get Out of Jail Tax Free

Tax professionals, like any specialist, tend to look at the world through the lens of their specialty. If you've ever watched a commercial and thought, ''But couldn't they deduct that?'' or pondered

Starker exchanges while watching Home and Garden Television, you know what I'm talking about.

So we weren't surprised when Robert Wood watched a little too much *CSI* and wondered about the tax consequences of winning a recovery after being falsely imprisoned. As he notes, there have been some large awards lately, and many states allow for recoveries. But surprisingly, the tax consequences of a recovery are not settled. Wood thinks the recovery shouldn't be taxable, but he thinks it wouldn't hurt if Congress clarified the issue. See p. 279 for his fascinating practice article.

Hedge Funds

In back-to-back news analyses, Lee Sheppard returns to the topic of hedge funds this week. In the first (p. 241), she analyzes the offer the Managed Funds Association recently pitched to Treasury: Hedge funds will buy up distressed mortgages as long as their foreign investors don't have to pay U.S. tax on the eventual gains.

In the second, Sheppard looks at the differences between how the United States and European countries treat the compensation of hedge fund managers' compensation. She notes that those countries treat compensatory transfers of partnership interests as compensation. So Europeans aren't baffled by the American tax treatment, they're jealous of it (p. 243).

IRS News

According to a report from the Transactional Records Access Clearinghouse (TRAC), IRS audits of large corporations dropped to an all-time low in 2007. Meanwhile, audits of small businesses have increased. TRAC is puzzled about why the Service would focus on smaller businesses when the large corporate audits net larger amounts of tax. The IRS maintains that the numbers have been manipulated and taken out of context, resulting in misleading conclusions (p. 247).

House and Senate appropriators grilled IRS Commissioner Douglas Shulman about private debt collection last week. A new estimate from the Joint Committee on Taxation says the program will raise $578 million over 10 years, which is almost half of the amount the JCT estimated last year. Shulman, who's been on the job for only a few weeks, said it was too early in his tenure to tell whether the program is meeting its purpose (p. 231).

The House, however, says the program isn't and voted again last week to yank the IRS's authority to enter into private debt collection contracts. The taxpayer assistance bill also includes a provision to require users of health savings accounts to document that any spending out of HSAs is health-related. President Bush has already issued a veto threat objecting to both provisions (p. 226).

More Commentary

In a special report, Tom Neubig and Estelle Dauchy expand on their previous special report (*Tax Notes*, Nov. 26, 2007, p. 873), which analyzed Ways and Means Chair Charles Rangel's corporate tax reform proposal. In this report, Neubig and Dauchy look at the effects the proposal would have on domestic-only corporations and update their prior report with an alternative analysis using a baseline that assumes an extension of several business credits (p. 289).

In a viewpoint, Profs. B. Anthony Billings and Buagu Musazi propose ways to maximize the incentive effects of bonus depreciation for the firms that most need it (p. 299). Lertlar Poopoksakul and Brett Southworth examine in Of Corporate Interest the tax aspects of stock conversion ratios (p. 305). And in letters, the authors of a recent article on Social Security (*Tax Notes*, Mar. 3, 2008, p. 1027) reply to letters about that article (p. 321).

Charles Kingson provides the latest installment in his series of Shelf Project proposals to reform the U.S. international tax rules. He says this proposal would create consistency for earnings, basis, and foreign tax credits on the sale of subsidiaries. Kingson didn't get the quote of the week, but he gets our line of the week for, "Check-the-box, which started out as a handmaiden to section 338, has now become its dominatrix" (p. 303). ■

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