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Use of computers in tax return preparation

American Institute of Certified Public Accountants. Tax Division. Tax Computer Applications Subcommittee

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AICPA Tax Division

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THE USE OF COMPUTERS IN TAX RETURN PREPARATION

PREFACE

Over the past twenty years, members of the accounting profession have become increasingly aware of the benefits derived from the use of computers by business enterprises and public institutions. These benefits (usually unobtainable from a manual system) have included speed and flexibility in processing data with relatively high accuracy, and have produced numerous informative analyses.

The availability of these benefits motivates CPA firms to consider using computers. However, because the means for utilizing electronic data processing are so varied and complex, even an experienced practitioner finds it difficult to evaluate the available options—service center, in-house computer (micro, mini or main frame), or some combination of both. For a novice, the task is virtually impossible.

This practice aid supersedes "Guidelines to Assess Computerized Tax Return Systems" developed by the Computer Applications Subcommittee and published by the AICPA in 1976. Many of the concepts and examples from the Guideline were very useful in developing this aid. This practice aid incorporates a number of issues not addressed in the 1976 Guidelines, including microcomputers, laser printers, and so forth.

INTRODUCTION

The purpose of this practice aid is to assist practitioners in assessing computerized tax return preparation applications.

Income tax preparation involves taking pertinent information, placing it on the appropriate tax form, and computing the lowest possible tax. Computing the lowest possible tax necessitates utilizing the appropriate rate tables as well as having the ability to compute the tax by using alternative methods.

Some of the advantages that can be gained by computerizing tax return preparation include—

- The saving of professional preparation time after the initial year by using computer-prepared pro formas.
- The ease of reprocessing a tax return with multiple schedules or forms that may be affected by changing one item.
- A more consistent tax preparation approach by all preparers within a firm by using uniform and structured methods and forms.
- The elimination of many arithmetic functions, resulting in the elimination of many arithmetic errors.
- The elimination of considerable repetitive handwriting (such as heading information).
- The increased efficiency of collecting and recording client tax information by using standardized input forms.
- A more rapid production of K-1s for partnership and fiduciary returns, which usually includes the automatic allocation of tax return items.
- The tax information data base may be utilized for various types of tax planning and analysis.

Some disadvantages include—

- The delay between submission of input forms and receipt of the completed tax returns. (If the returns are prepared off-premises, a delay near the filing deadlines may be particularly harmful.) This disadvantage may be mitigated by processing in-house.
- The separate manual preparation of state or city returns when unavailable from the computer system used. (An in-house system may not have as many state return programs available as an off-premises service.)
- The inability of a computer system to generate and/or print certain forms.
- Less data security when processing occurs off-premises.
- Unrecoverable costs (for example, caused by reruns) resulting from input errors.
- Capital costs in the form of hardware, software and training.

All examples used in this practice aid were in effect at the time of its publication. Some of these examples will eventually become obsolete, but, regardless of changes in tax law, the concepts will remain valid.

COMPUTER TAX RETURN CHARACTERISTICS

This practice aid presents the characteristics of computerized tax preparation that are considered to be the minimum specifications for acceptability, or the capabilities or features that are essential to complete the basic mission of the system. The need for such features is unchanging; that is, no matter how procedures are modified, the conditions requiring the features will almost always be present. The features cannot be ranked, because lacking any one feature the system would fail to complete its required mission.

The practice aid also points out some additional available features that, though unnecessary for providing the minimum capabilities for a tax return system, should nevertheless be considered. Conversely, the absence of any one of these items should not be a significant consideration.

These additional features have the following characteristics:

- The inclusion of the feature would improve the system's performance.
- The feature would provide a capability above and beyond a particular minimum feature.
- The features may be ranked by desirability.
- The features represent desirable items that are moderately priced.
- The features, which can differentiate between systems, form the basis of selection among eligible systems (that is, systems meeting the minimum specifications).

PRO FORMAS

The data that appear on a tax return may be divided into two categories: (1) information related only to the period to which the return applies and (2) information also applicable to future-period returns. The ability of computers to retrieve stored information both quickly and economically is used in tax return preparation by preparing *pro formas*. The term pro forma refers to input sheets upon which the computer has printed prior-period recurring information. The information has been computer-stored, and, by utilizing the computer to print that information on the input sheets, repetitive handwriting is eliminated.

Typically, the following types of information are produced on a pro forma:

- Taxpayer information (name, address, identification numbers, occupation, and so forth)
- Listings of sources from which dividends and/or interest are received
- Depreciation information

Examples of pro formas follow.

EXAMPLE 1—TAXPAYER/SPOUSE GENERAL INFORMATION

Taxpayer's First Name and Initial	Spouse's First Name and Initial	Last Name		
ROBERT R.	RUTH S.	BOULDER		
Street: 1201 CRESTVIEW	City: ANYTOWN		Taxpayer Year of Birth (4 Digits)	Spouse Year of Birth (4 Digits)
State: ANYSTATE	Zip Code: XXX13	County: JACKSON		
Taxpayer's Soc. Sec. Number: 212 304 769	Taxpayer's Occupation: SALESMAN			
Spouse's Soc. Sec. Number: 331 269 611	Spouse's Occupation: BROKER		1932	1932

Dependent Children Who Lived With You

Enter Total No. of Children Claimed		
	Taxpayer: 2	Claimed by Taxpayer: JAMES, KENNETH
	Spouse	Claimed by Spouse

EXAMPLE 2—DIVIDENDS

	t s j	Qualifying Portion		Nonqualifying Portion		Capital Gain Portion		Nontaxable Portion	
* AMERICAN ELECTRIC POWER CO., INC.	T								
* AMERICAN GENERAL BOND FUND, INC.	T								
* BARNES MORTGAGE INVESTMENT TRUST	T								
* DAYTON HUDSON CORP.	S								
* EXXON CORPORATION	S								
* HOTEL INVESTORS	J								
* ILLINOIS POWER COMPANY	J								
* NATURAL GAS PIPELINE CO. AMERICA 7.10	T								
* PUBLIC SERVICE ELECTRIC & GAS CO.	T								

*This part is computer-printed.
t=taxpayer
s=spouse
J=joint

In some systems, prior year amounts are shown on the pro formas to help the preparer to complete the input forms, as in example 3 below.

EXAMPLE 3—CONTRIBUTIONS

t s j		Amount		Prior Year
T	*HIS UNIVERSITY			200.00*
J	*UNITED WAY			15.00*
J	*OUR CHURCH			125.00*
S	*HER ALMA MATER			200.00*

This part is computer-printed. Total Contributions 540.00

In some systems, the prior year amounts are produced in booklet form to be used by the client to help in the collection of the current year's information. Example 4, extracted from such a client data gathering booklet, follows.

EXAMPLE 4—CONTRIBUTIONS IN BOOKLET FORM

DESCRIPTION	CURRENT YEAR	PRIOR YEAR
*(T) HIS UNIVERSITY		200.00*
*(J) UNITED WAY		15.00*
*(J) OUR CHURCH		125.00*
*(S) HER ALMA MATER		200.00*
*This part is computer-printed.	Total Contributions	540.00*

MINIMUM SCHEDULES AND FORMS

When manually preparing tax returns, even if seldom used, all necessary tax forms are usually available. However, when utilizing a computer, only those forms prepared by the system being used are available. The computer tax return vendors determine which forms they will offer by reviewing their customers' demands and usage. Ordinarily, the computer services will prepare schedules and forms that handle a large percentage (perhaps all) of a practice's requirements. As a minimum requirement for acceptability, any computer tax preparation system must provide the forms that are generally applicable to all taxpayers.

STATE FORMS

The preparation of state and local tax returns may be considered a minimum requirement. The capability of preparing such returns is available in specific systems and should be considered in evaluating the applicability of computerized tax return preparation for a practice.

ADDITIONAL FORMS

While some services do not provide for all forms, they will allow for input of the corresponding results so that a complete tax computation can be made. If only totals are used for input, the preparer must complete the form in a manner that will allow it to be included with the filed return.

MINIMUM PROCESSING SPECIFICATIONS

In addition to minimum schedules and forms, the following are certain processing characteristics considered minimum for an acceptable computer tax return system:

- The calculations performed by the system must reflect the present legislative, regulative, and administrative requirements of federal, state, and local taxing authorities.
- Every sheet of output must show the taxpayer's name and identification number. Not only is this particularly important for in-house processing to facilitate collating, but it is also important if pages are inadvertently separated in the government's processing centers.
- The system should provide for storage of taxpayer information to enable the preparation of pro forma input sheets for subsequent tax periods.
- All supporting schedules must be identified and referenced to the corresponding form.
- All of the currently published government specifications for forms must be met, especially for the sections applicable to preprinted or substitute forms.
- The system should calculate depreciation using appropriate methods.
- The system should have the capability of producing multiple copies of the return.

ADDITIONAL PROCESSING FEATURES

Certain features may be present in computerized tax preparation systems and should be taken into consideration when evaluating alternative systems of tax return preparation. Some of these features, which may be considered minimum processing specifications, include:

- A listing of the schedules and forms prepared for each taxpayer.
- A letter of transmittal to the client containing all filing instructions.
- Availability of forms (usually produced as a booklet) designed to help the client to both collect and record the information needed in the preparation of the current year's return (for example, a listing of the prior year's information and amounts with space available to enter the corresponding data for the current period).
- The sale of a group of assets at one price that enables the preparer to request automatic allocation among sections of that selling price.
- Preparation of fiscal year returns with required pro rata calculations.
- Limited cash flow statements that show income and itemized deductions with amounts and percentages.
- A work sheet comparing the various methods (for example, itemized deductions, standard deduction, and so on) used to calculate income tax.
- The automatic calculation of gains and losses, including ordinary income recapture, that results from the sale of depreciable assets.
- The preparation of worksheets (for both tax and financial planning) that can include comparisons of current to prior year's data.
- The ability to produce practice management aids, including client billings, mailing labels, and so forth.
- The ability to link with other computer applications.
- A system that meets the requirements of electronic filing.

PRACTICE PROFILE WORK SHEET

The tax return schedules and forms needed in a practice, and the total usage of each, are major determining factors in evaluating alternative computerized tax return methods. Accordingly, to obtain an overview of a particular tax practice, it is imperative to review representative clients' tax return files. By recording the forms included in a client's returns, a tally of the forms used in the practice can be produced. A Practice Profile Work Sheet has been included in appendix 1 to aid in the survey of forms used with individual tax returns.

Example 5, below, illustrates the use of the work sheet. Of the three hundred returns in the example, over 20 percent require Schedules A, B, C, D, E, SE and ES and Form 4562. Thus, this sample CPA practice should set the availability of these schedules as a minimum requirement for accepting a computerized tax return system.

The work sheet is designed to determine a practitioner's use of individual tax return forms. A similar approach (though without the variety of forms) can be utilized for corporate, partnership, and fiduciary tax preparation.

EXAMPLE 5—EXAMPLE OF A PRACTICE PROFILE WORKSHEET

		SCHEDULES										FORMS												
NAME	IDENTIFICATION NUMBER	A	B	C	D	E	F	G	R	SE	ES	1116	2106	2119	2240	2441	2468	3903	4136	4255	DEPR	4625	4797	4798	5329
William Abbot	123-45-6789	X	X												X										
James Baker	111-22-3333	X									X														
Michael Bates	222-33-4444	X	X														X								
Alex Craft	333-44-5678	X	X	X	X					X	X	X					X				X		X	X	
Steven Fox	434-55-6789			X							X									X					
David Gary	545-45-4545	X	X					X		X			X				X								
Thomas Henderson	666-77-8886				X	X		X			X							X							
David Larson	707-07-0707	X	X	X													X				X				
Paul Simon	007-00-7007	X	X			X											X								
Fred Wright	999-99-9999	X	X			X	X			X	X						X		X		X				
300	TOTALS	240	219	90	61	93	32	62	8	94	89	7	41	–	13	6	–	92	10	32	19	122	–	–	10	10

PROCESSING CONSIDERATIONS

This section presents processing considerations as they relate specifically to computerized tax return preparation.

DOCUMENTATION

The nature and scope of system documentation will be determined by the choice of operating modes. Preparing tax returns in-house will necessitate documentation regarding the operation of the computer itself, while processing through a service center may restrict documentation to input forms and the output received. Each area of system documentation must be clear and concise, updated when necessary, and understandable to all users, whether they are preparers of input forms, reviewers of returns, or other personnel involved in system operations.

TECHNICAL SUPPORT

Whatever type of system is used, technical support from vendors or developers of the system should be readily available. The more complex the system, the more important this support becomes. Technical support should include both system operation as well as tax-oriented information.

SECURITY

As with all information in a practitioner's office, client information, which is necessary for tax return preparation, must be kept confidential. Therefore, security must be evaluated regardless of whether an in-house system or an outside service is used. Security measures must include proper disposal of input and output forms that may contain taxpayer data, proper control of collating and mailing returns, and safe retention of client data.

If service centers are used, physical and data security measures should be ascertained. To maintain continuity of processing capabilities, the service center should have both back-up facilities and off-site data storage. The practitioner should implement input controls for both delivery and output receipt.

If an in-house system is used, the maintenance of back-up copies of machine-readable data files is critical, and these back-ups should be kept at an off-site storage facility.

TRAINING

Proper training of all users of the tax-processing system is best accomplished when adequate documentation and support are provided by the system's vendor. Tax return preparers, data-processing personnel, clerical staff, and review personnel should be thoroughly familiar with their duties to accomplish proper, efficient processing.

PROCESSING THROUGHPUT (TURNAROUND)

The throughput capability of a system is the rate at which it can receive input, perform processing, and produce finished output. The evaluation of an in-house facility for tax return processing should include a determination of throughput capability. Consideration of service center processing would necessitate determining the turnaround time (time between submission of input and receipt of output). When evaluating the throughput of the alternative methods of computer tax return processing, the following elements are to be considered:

- Delivery time
- Ability to expedite processing returns as the filing date approaches
- Cutoff dates under the various options
- Time and effort involved in handling forms

SUPPLIES

Forms for initial data entry, pro formas, instruction manuals, preprinted output forms, and all other necessary supplies must be available on a timely basis. The design of forms should reflect a logical and clear presentation, and include, where applicable, totals and other control data. If input sheets are to leave the premises, some practitioners may duplicate the input sheets and retain one copy for in-house purposes.

PROCESSING OPTIONS

The alternatives for processing tax returns by computer are (1) an in-house system, (2) service centers, and (3) a mixture of service center and in-house systems.

Below are the descriptions of these processing methods as well as their advantages and disadvantages. Each practice is unique, and, therefore, an evaluation should be made of every processing option within the practice's parameters and requirements.

IN-HOUSE SYSTEM

With the in-house processing option, data processing equipment is acquired through rental or purchases. The practitioner's firm assumes full responsibility for input, data security, turnaround time, and output collating. In using the in-house method, the practitioner's firm must bear rerun costs. (In other methods, the computer tax service could bear certain rerun costs. Some commercial services offer at no cost reruns before an early date to entice earlier submission of input in order to spread peak processing.)

Advantages

The following advantages can result from using the in-house system option.

Input:

- Source documents do not leave the premises; therefore, privacy is maintained.
- Client data is entered directly into an in-house system, thereby avoiding the transcription of client data onto input forms.

Processing:

- Priorities of all processing can be modified to produce an operation that is not only the most efficient possible, but also the most responsive to requirements of both the installation and the practice unit.

Output:

- Turnaround time is fully dependent on, and under the direct control of, the practitioner's firm.

Costs:

- Tax return processing can utilize unused computer time.
- There is a profit potential through expanded services to clients, and, with a large volume of returns, per-return costs can become low enough to increase profits. Additional profits can be earned by processing returns for other practitioners and/or attorneys.

Disadvantages

When considering the in-house processing option, scheduling is an important factor. The bulk of tax return processing is concentrated in a seventy-five-day period (February 1–April 15). If computer time is not available because of other processing commitments, then the costs of personnel overtime and possible additional computer rental may cause the practitioner to consider using one of the other processing modes discussed below.

Besides scheduling, other disadvantages include the following.

Processing:

- Programs available to in-house users are usually less sophisticated than timesharing or service center options. If microcomputers and laser printers are used, then a combination of service center and in-house can be advantageous.
- Not only is the availability of acceptable programs limited, but a firm must also rely on the software vendor to supply timely updates and maintenance.
- Security and data back-up become the practitioner's responsibility.

Output:

- All forms handling must be done by the CPA firm.

Costs:

- There may be a high fixed-cost as well as an equipment commitment.
- If equipment is installed, there may be physical facilities requirements.

However, if a practitioner maintains an in-house installation, then the equipment commitment has been made, and the space requirements are already met. Therefore, as additional costs for equipment and space are no longer required, these two cost disadvantages become advantages.

As in every other computer application, the in-house user has the option to purchase, rent, or develop internally operable computer programs (software). Tax return law is complex, and its reduction to computer programs is time-consuming and, thus, expensive. The resulting development cost is often too great for one firm to bear, and, therefore, tax return programs used on in-house equipment are usually either purchased or leased.

SERVICE CENTERS

A service center is a company that provides data-processing services. A wide variety of service arrangements are available, including the conversion of input data to machine-readable form, processing the data, and physically delivering the output to the customer. In addition, in order to meet special requirements, a service center may offer system design and programming support.

The usual procedure is to send input to the service center in the form of input sheets. However, if supplied with input in machine-readable form, many service centers will reduce their fees.

Comparisons between service centers can be easily made. The evaluation, however, becomes subjective because each practitioner may have preference for certain types of input forms, and the cost of each system must be weighed against the additional forms and features offered.

In order to resolve users' questions, many service centers offer problem solving either by on-line terminal or by telephone. Although the answer to a particular question is usually found in the instruction manual, some practitioners believe that the phone call cost is more time-efficient.

Advantages

The advantages to using service centers include the following:

Input:

- A good instruction manual is usually available for users.
- "Pro forma" input data, which speeds the input process, is available.

Processing:

- Generally, the tax return programs are as sophisticated as any offered.
- Equipment requires little or no space.
- More complete services have a wide range of forms available for partnerships, corporations, fiduciaries, and many local individual tax returns.
- In some cases, returns can be traced, reviewed, and changed by telephone.

Output:

- Returns are delivered to the firm collated in the proper sequence and require minimum handling.

Costs:

- No capital investment is necessary.
- Fixed costs are low. (Charges are only for schedules and forms prepared.)

Disadvantages

The following are the disadvantages to using service centers.

Input:

- Client information leaves the practitioner's office, and, despite precautions, may be subject to unauthorized access and/or use.

Processing:

- The processing center assumes limited responsibility. The practitioner assumes the same responsibility for correct processing—as if processing were to take place in-house.

Output:

- Turnaround time is not only dependent on the service center, but, in most cases, on postal delivery as well. (Many services have alleviated this disadvantage by instituting a courier service that charges by location.)

Costs:

- The reprocessing of tax returns generally incurs additional costs with longer turnaround time.

COMBINATION OF SERVICE CENTER AND IN-HOUSE SYSTEM

For some practitioners, an approach that may provide the best answer is a combination of service center and in-house systems. A key feature of this approach is the flexibility in the selection of processing methods on a return by return basis. In this approach, the practitioner is responsible for inputting into a microcomputer the client's data, which is then telecommunicated to a service center. After processing the information, the service center may either print the tax return or transmit the data back to the practitioner for printing (typically on a laser printer). Prior to printing, the practitioner may then "inquire" into the tax return information, and, after the tax liability is known, input changes back into his in-house microcomputer.

Advantages

The use of a combination of service centers and an in-house system can produce the following advantages.

Input:

- Since the source document does not leave the practitioner's premises, its privacy is maintained.
- Many input errors may be immediately indicated.

Processing:

- The tax return programs are usually as sophisticated as any offered.

Output:

- Turnaround time is short.
- The return may be printed either in-house or at the service center.

Costs:

- The setup and fixed costs are relatively minimal.

Disadvantages

The following are some of the disadvantages to the combination approach.

Input:

- Although transmission difficulties seldom arise, the user should be aware that both transmission interference and corresponding data loss can occur.

Processing:

- The practitioner is responsible for ensuring that the in-house element of the software is the most current release.

Output:

- If a typewriter-like printer is used, output is usually on blank paper, which requires overlays to simulate government forms.
- The variable costs associated with a service center may be greater than the relatively fixed costs associated with an in-house system.

APPLICATION PROCESSING

INPUT

The organization of the input forms or data entry screens are of prime importance. Although most input preparers are conversant with taxes, a large percentage, however, are not familiar with computers. Therefore, the language gap between tax preparation and computer processing should be bridged by instruction manuals, which are in tax-preparer language, and input sheets.

After the input is prepared, and before it is submitted for processing, both its accuracy and completeness should be reviewed. In addition, there should be a professional review of the input data. In-house processing requires total control checks. The practitioner who uses off-premises services should review input data before transmitting it to the service center as well as ascertain what type of reviews the service performs.

PROCESSING

Controls. The computer should be programmed to check for compliance with statutory requirements. For example, the limits on contributions and medical expenses should not be exceeded. In addition, a computer tax return program should contain checks for both reasonableness and the possible omission of certain input data, such as when—

- Interest and/or taxes on rental property are zero.
- Depreciation is not taken on business, farm and/or rental operations.
- Prior depreciation was omitted for an asset with an acquisition date before the first day of the current tax year.

When running an in-house system, the practitioner should ask the software vendor to provide a listing of the limit checks and reasonableness checks that the system uses.

Reprocessing. The necessity to reprocess tax returns largely arises from corrections or revisions made in the initially submitted taxpayer information. The system should be designed so that reruns will require modification of only the original data, rather than a second complete data conversion of all the information from input sheets to machine-readable media. Any processing requires an understanding about rerun procedures between the tax personnel and the computer personnel. Those procedures should be defined and adequately documented in both the preparation and the operation manuals.

Software. When determining which processing avenue to take, both the dollar costs and the level of the program's sophistication should be considered (for example, how much must the practitioner do to prepare the return, and how much will the computer do). As in the case of any data-processing application, the functions provided by a tax preparation application will be limited by the capabilities of the computer used to process the application.

If a minicomputer or microcomputer is used as an in-house system, a firm may find that its computer has limited capabilities. An investigation must be made to see what level of

sophistication the available programs reach, and how much calculation and arithmetic work the programs actually do. The best programs produce maximum output from minimum input and require the least work to determine the lowest tax. Input is minimized by a system that can spread information from one input sheet to all applicable forms.

OUTPUT

For in-house processors, the use of laser printers could diminish the large bottleneck created by paper handling. After processing, time and effort are involved in bursting and collating the burst sheets into IRS-required order. Although bursting can be done by special machines, some capital investment may be required. Nevertheless, many in-house processors insist that collating can only be done manually. The cost and importance of collating is, therefore, another consideration in whether tax returns should be done on an in-house computer.

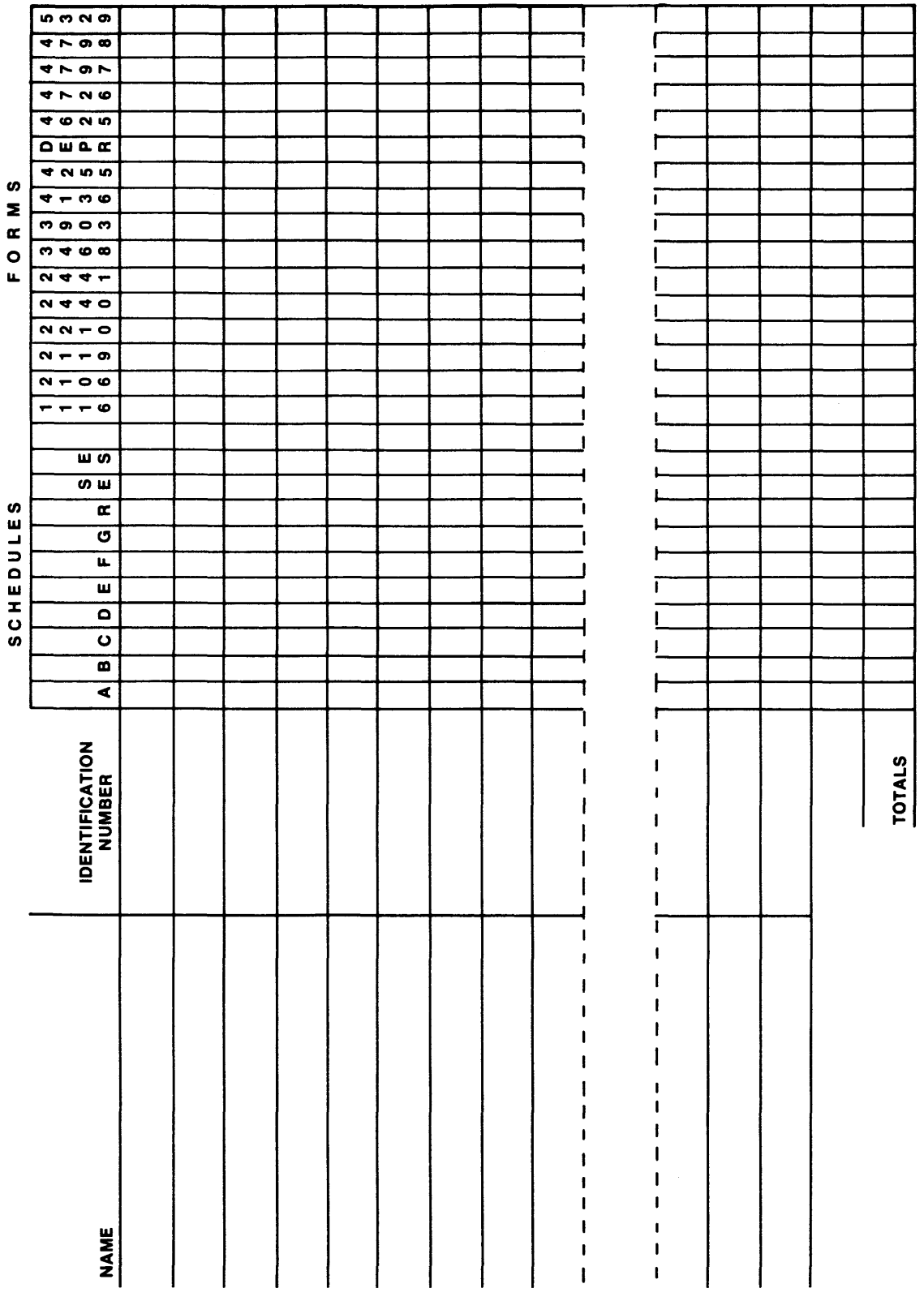
USING THE APPENDIXES

In order to apply the evaluation criteria presented in this practice aid, three appendixes are included: appendix 1, "Practice Profile Work Sheet"; appendix 2, "Computer Tax Preparation Checklist"; and appendix 3, "Cost/Benefit Analysis Work Sheet."

These appendixes offer a basis for comparing sources of tax return processing.

Appendix 1

Practice Profile Work Sheet



Appendix 2

Computer Tax Preparation Checklist

Minimum features are essential to any acceptable system. Therefore, the absence of one minimum feature should disqualify a system.

Part 1 is a checklist of the minimum features in a computerized tax preparation system. Provision is made in items 1–3 for inserting additional forms that the CPA considers essential for a tax practice and, therefore, should be considered additional minimum features.

Part 2 is a checklist of additional features that should be considered in evaluating several systems that have met the minimum requirements. Values should be assigned to the additional features to assist in making a quantitative evaluation.

Column A requires a judgment of the importance of a feature on a scale of:

0 Never used
1 Used 25 percent of the time
2 Used 50 percent of the time
3 Used 75 percent of the time
4 Used almost all the time

Column B calls for a judgment of how completely a feature is provided on a scale of:

0 Not provided
1 Provided but requires extensive manual input
2 Provided but requires minimal manual input
3 Provided completely

Part 3 is a checklist of other processing considerations that the CPA is to consider in selecting a system that has met the minimum specifications.

Column A requires a judgment of the importance of the feature on a scale of:

0 Not important
1 Partially important
2 Very important

Column B calls for a judgment of how completely a feature is provided on a scale of:

0 Not provided
1 Some provided
2 Half provided
3 Almost completely provided
4 Completely provided

Appendix 2 *Continued*

1. Minimum Features 1-1. Does the system provide the following schedules and forms?	Individuals	Corporations	Subchapter "S"	Partnerships	Fiduciaries	Yes	No
(a) Basic form	X	X	X	X	X	___	___
(b) Schedule A—Itemized Deductions	X					___	___
(c) Schedule B—Dividend and Interest Income	X					___	___
(d) Schedule C—Profit or (Loss) from Business or Profession	X					___	___
(e) Schedule D—Capital Gains and Losses	X	X	X	X	X	___	___
(f) Schedule E—Supplemental Income Schedule	X					___	___
(g) Schedule F—Farm Income and Expenses	X			X		___	___
(h) Schedule G—Income Averaging	X					___	___
(i) Schedule J—Allocation of Accumulation Distribution					X	___	___
(j) Schedule K-1—Share of Income, Deductions, Credits, etc. (Form K-1 should be available as either an automatic allocation or by an allocation provided on input sheets.)			X	X	X	___	___
(k) Schedule R—Retirement Income Credit Computation	X					___	___
(l) Schedule SE—Computation of Social Security Self-Employment Tax	X					___	___
(m) Schedule ES—Estimated Tax Payments	X					___	___
(n) Form 2210—Underpayment of Estimated Income Tax by Individuals	X					___	___
(o) Form 2220—Underpayment of Estimated Income Tax by Corporations		X				___	___
(p) Form 4625—Computation of Minimum Tax	X					___	___
(q) Form 4726—Maximum Tax on Earned Income	X				X	___	___
(r) Form 4797—Supplemental Schedule of Gains and Losses	X	X	X	X	X	___	___
(s) Form 5329—Return for Individual Retirement Savings Account	X					___	___

1-2. Does the system provide the following processing features?

	Yes	No
(a) Calculations reflecting present income tax laws	___	___
(b) Taxpayer's name and identification number on every output sheet	___	___
(c) Pro forma input sheets	___	___
(d) Supporting schedules properly indexed and referenced	___	___
(e) Forms printed according to government specifications	___	___
(f) Federal tax returns in the collating sequence prescribed by the IRS	___	___
(g) The required number of copies	___	___

1-3. Does the system provide the following other features which are essential to the firm's tax practice needs?

(a) _____	___	___
(b) _____	___	___
(c) _____	___	___
(d) _____	___	___

2. Additional Features

2-1. Does the system provide the following other forms?

	Individuals	Corporations	Subchapter "S"	Partnerships	Fiduciaries	A Relative Importance (0-4)	B Extent Provided by System (0-3)	C System Evaluation Score (AxB)
(a) Form 1116—Computation of Foreign Tax Credit	X				X	___	___	___
(b) Form 1118—Computation of Foreign Tax Credit		X				___	___	___
(c) Form 2106—Employee Business Expenses	X					___	___	___
(d) Form 2119—Sale or Exchange of Personal Residence	X					___	___	___
(e) Form 2440—Sick-Pay Exclusion	X					___	___	___
(f) Form 2441—Expenses for Household and Dependent Care Services	X					___	___	___
(g) Form 2555—Exemptions of Income Earned Abroad	X					___	___	___
(h) Form 3468—Computation of Investment Credit	X	X		X	X	___	___	___

(Continued)

Appendix 2 *Continued*

	Individuals	Corporations	Subchapter "S"	Partnerships	Fiduciaries	A Relative Importance (0-4)	B Extent Provided by System (0-3)	C System Evaluation Score (AxB)
(i) Form 3903—Moving Expense Adjustment	X					___	___	___
(j) Form 4136—Computation of Credit for Federal Tax on Gasoline, etc.	X	X			X	___	___	___
(k) Form 4137—Computation of Social Security Tax on Unreported Tip Income	X					___	___	___
(l) Form 4255—Tax from Recomputing a Prior-Year Investment Credit	X	X			X	___	___	___
(m) Form 4798—Capital Loss Carryover	X					___	___	___
(n) Form 4831—Rental Income	X					___	___	___
(o) Form 4972—Five-Year Averaging Method for Self-Employed Individuals	X					___	___	___
(p) _____						___	___	___
(q) _____						___	___	___
(r) _____						___	___	___
(s) _____						___	___	___
(t) _____						___	___	___
(u) _____						___	___	___
(v) _____						___	___	___
(w) _____						___	___	___
(x) _____						___	___	___
(y) _____						___	___	___

2-2. Does the system provide the following other processing features?

(a) Automatic sales tax calculation	___	___	___
(b) Gasoline tax deduction based on miles	___	___	___
(c) Depreciation calculation on all allowable methods	___	___	___
(d) Preparer-selected switch of depreciation from accelerated to straight line	___	___	___
(e) Capital loss carryover calculation	___	___	___
(f) Investment credit carryover calculation	___	___	___
(g) Net operating loss carryback/ carryover calculation	___	___	___

	A Relative Importance (0-4)	B Extent Provided by System (0-3)	C System Evaluation Score (AxB)
(h) Carrying depreciable asset information to the investment credit and/or recapture of investment credit forms from the depreciation input	___	___	___
(i) Installment sales percentage calculations	___	___	___
(j) Listing of prepared schedules and forms by taxpayer identification number	___	___	___
(k) Filing instruction letter	___	___	___
(l) Subsequent-year interview information	___	___	___
(m) Depletion allowance computation	___	___	___
(n) Allocating selling price for Form 4797 on bulk sale of assets	___	___	___
(o) Fiscal year returns with pro rata calculation (usually corporate and partnership)	___	___	___
(p) Limited cash flow statements	___	___	___
(q) Income tax results by different methods	___	___	___
(r) _____	___	___	___
(s) _____	___	___	___
(t) _____	___	___	___
(u) _____	___	___	___
(v) _____	___	___	___
(w) _____	___	___	___
(x) _____	___	___	___
(y) _____	___	___	___
3. Other Processing Considerations			
3-1. Will the provided operating documentation meet your needs?	___	___	___
3-2. Are the security measures for client information adequate?	___	___	___
3-3. Is the training provided sufficient to meet your needs?	___	___	___

(Continued)

Appendix 2 *Continued*

	A Relative Importance (0-4)	B Extent Provided by System (0-3)	C System Evaluation Score (AxB)
3-4. Will all supplies be available on a timely basis?	___	___	___
3-5. Is turnaround time acceptable?	___	___	___
3-6. Are the input forms easy for the preparer to understand?	___	___	___
3-7. Are the instruction manuals comprehensive and understandable?	___	___	___
3-8. Before processing, does the system provide for review of the input forms for unacceptable coding (entries)?	___	___	___
3-9. Does the program check for compliance with statutory requirements?	___	___	___
3-10. Does the program have checks for reasonableness?	___	___	___
3-11. Does the program check for omission of related input items?	___	___	___
3-12. Are rerun responsibility and cost defined?	___	___	___
3-13. Will sufficient repetitive data be available on next year's pro forma?	___	___	___
3-14. Can paper handling problems be minimized?	___	___	___
TOTAL			

Appendix 3

Cost/Benefit Analysis Work Sheet

In this work sheet, a method to establish dollar values for alternative tax preparation systems is provided. The section entitled "Direct Costs of Tax Return Processing" pertains to costs that are incurred only for tax return processing. Large volumes of tax return processing are a seasonal activity. Therefore, it is expected that pay for either overtime or temporary employees can be directly attributed to tax return processing; whereas, regardless of their activities, permanent, full-time employees will always be paid. Similarly, the recording of direct costs of equipment should be for additional equipment needed; that is, overtime rent on in-house systems or leased equipment for tax return processing (terminals, block-time, typewriter, etc.). Duplicating equipment costs can be precisely identified when the firm reproduces extra copies of handwritten or typed returns. The remaining items of direct incremental costs are to be treated with the same concept (costs incurred only for tax return processing).

By subtracting present method costs from the alternative system's direct costs, the savings, if any, can be determined.

The second section, "Potential Benefits of Alternative Systems," requires judgments by the CPA in the dollar value of improved productivity, service, and capability. For example, if professional time can be saved, will the professional leave work sooner or do other billable work? If the same professional leaves work sooner, what is the value of improved morale, fresher personnel, and so on? Will staff productivity increase by 10, 20, 30, or 50 percent, thus enabling the firm to take on more billable work? These individual judgments and assigned dollar values are to be added to the direct cost savings that would result in total savings and benefits.

WHENEVER SYSTEMS ARE CHANGED, THERE WILL ALWAYS BE SIGNIFICANT CONVERSION COSTS. These costs should be amortized and subtracted to arrive at net savings (costs) and benefits from the alternatives.

COST/BENEFIT ANALYSIS WORK SHEET *(page 1)*

	ESTIMATED ANNUAL COSTS/BENEFITS					
	PRESENT SYSTEM	ALTERNATIVE SYSTEMS				
DIRECT COSTS OF TAX RETURN PROCESSING		(1)	(2)	(3)	(4)	(5)
Personnel:						
Overtime						
Temporary help						
Data-Processing Equipment:						
Accounting machine or computer						
Data entry devices (e.g., keypunches)						
Terminal devices						
Communication devices						
Duplicating Equipment						
Assembly Equipment (e.g., collator)						
Storage Equipment						
Supplies:						
Input forms						
Output forms						
Computer media (e.g., tapes, disks)						
Computer Software and/or Programming Expense						
Service Center or Timesharing Fees						
Total Direct Cost		( )	( )	( )	( )	( )
Present System Costs	↳					
Direct Savings (Expense) (A)						

COST/BENEFIT ANALYSIS WORK SHEET *(page 2)*

	ESTIMATED ANNUAL COSTS/BENEFITS					
	PRESENT SYSTEM	ALTERNATIVE SYSTEMS				
POTENTIAL BENEFITS OF ALTERNATIVE SYSTEMS		(1)	(2)	(3)	(4)	(5)
Increased Professional Staff Productivity:						
Preparer training						
Client interview						
Research						
Input preparation						
Return preparation						
Conceptual tax review						
Clerical accuracy review						
Ease of making changes						
Elimination of duplicate manual entries						
Subtotal						
Increased Clerical Staff Productivity:						
Interview material typing						
Data entry (e.g., keypunching)						
Return typing						
Return reproduction						
Return assembly						
Instruction typing						
Filing						
Subtotal						

(Continued)

COST/BENEFIT ANALYSIS WORK SHEET *(page 3)*

	ESTIMATED ANNUAL COSTS/BENEFITS						
	PRESENT SYSTEM	ALTERNATIVE SYSTEMS					
Improved Client Service:		(1)	(2)	(3)	(4)	(5)	
Consistent preparation approach							
Assured mathematical accuracy							
Automatic tests of tax alternatives							
Faster turnaround time							
Better final product appearance							
Subtotal							
Improved Management Capability:							
Better staff scheduling							
Avoidance of peak load problems							
Control of return preparation cost							
Improved reaction to client needs							
Subtotal							
Total potential benefits (B)		( )	( )	( )	( )	( )	
Present system benefits	↳						
Total direct benefits							
Total savings and benefits (A+B)							
Less amortized conversion costs[7]							
Residual savings and benefits							

[7]See Form 4 (p. 25) in *Guidelines for General System Specifications for a Computer System.*