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Does E-filing Taxes Lead to Increase in Identity Theft?

E-filing your tax returns has many advantages like speedier tax refunds. Over the last few years, there has been a surge in the percentage of taxpayers who e-file their tax returns. Last year, a total of 71% of American taxpayers used the e-filing system to submit their tax returns. At the same time, there has also been a massive increase in the number of identity thefts in relation to taxes. The number of tax-related identity theft incidents has increased fivefold, from about 50,000 in 2008 to nearly 250,000 in 2010, out of about 140 million returns. Are the two increases linked?

According to IRS Commissioner Doug Shulman, the two increases have happened by coincidence and there is no evidence of them being linked. In statements made by Shulman to the House Oversight and Government Reform Committee's panel on financial management, he said that e-filers are required to submit all the same information as paper filers but that does not mean it is more difficult for identity theft to occur because of the physical forms used by paper filers. The identity thieves would simply claim to have lost their forms. Furthermore, the fraudsters can receive refunds just as quickly as e-filers by submitting paper returns by overnight mail.

The director of a Government Accountability Office (GAO) review of identity theft, Jim White agreed that there is no evidence that the increase in identity theft cases is due to breaches in the IRS security systems, whether physical or online. Nevertheless, he said that it would be worthwhile for the IRS to learn more about the number of identity thieves who e-file fraudulent returns or who request that refunds be paid out to debit cards rather than in paper checks or direct deposits to checking accounts as this could help the IRS to increase their rate of fraud detection.

The most common form of tax-related identity theft is where the thief assumes another taxpayer's identity to submit a tax return and claim a tax refund. Another common form is what is known as employment fraud where an identity thief who doesn't want to apply for a job with his own record will provide someone else's name and information to do so.

To address the situation, the IRS has put into practice a series of automatic triggers that raise a red flag, such as a major change in income. This would automatically result in additional inspection. Returns from past victims of tax-related identity theft also automatically undergo additional inspection.