



New Split Refund Option: Purchase U.S. Savings Bonds

The IRS has announced that tax filers may directly purchase U.S. Savings Bonds in 2010 with their tax refunds. Filers will now be able to check off on their tax return that they want to use part of their tax refund to electronically purchase Savings Bonds. This is a new feature of the IRS split refund policy.

What are split refunds?

The IRS provides the “split refund” option to enable tax filers receiving a refund through direct-deposit to allocate portions of the refund directly into as many as three different accounts. This is designed to make it easier for tax filers receiving substantial refunds, such as from the EIC and CTC, to take advantage of savings and asset development opportunities at the same time they file their return. Using the split refund option, a filer could directly deposit part of a tax refund into a savings account, part into an Individual Retirement Account, and the remainder into a checking account. If they use this option, filers may not receive the balance of their refund as a paper check mailed by the IRS.

Purchase Savings Bonds through a split refund

When filing a return in 2010, filers choosing to split their refunds may now choose to purchase Savings Bonds and deposit the rest of the refund into as many as two other accounts. While Savings Bond purchasers normally have to establish an

account with the U.S. Department of Treasury in order to make a purchase, this preliminary step is not necessary when using the split refund option. The Treasury Department will mail the bonds directly to the filer. Pilot tests at free tax assistance sites in 2009 found that Savings Bonds were a popular and trusted savings option for taxpayers who might otherwise be reluctant to establish a savings account or Individual Retirement Account. The IRS provides a fact sheet on using a tax refund to purchase Savings Bonds at: www.irs.gov/pub/irs-tege/ibond_questions_answers.pdf.

Individuals often wish to purchase Savings Bonds in the name of a child or grandchild. This may not be done using the split refund tax return option in 2010, but will be possible in 2011.

Taxpayers should understand that while Savings Bonds are a risk-free investment, they are a long-term savings vehicle. They generally cannot be redeemed within a year of initial purchase, unless the owner lives in a disaster area. If the owner redeems a Savings Bond within five years of purchase, he or she loses the most recent three months of interest.

What are the benefits to splitting a refund?

Lower-income workers have many demands on their modest incomes and often lack a bank account in which to deposit savings. Receiving a large lump-sum EIC and CTC refund that averages over \$2,000, and for some is over \$5,000, provides an incentive to save, but most workers are reluctant to commit their entire tax refunds to savings.

The split refund option provides lower-income workers a convenient automatic savings mechanism that can facilitate their decision to save some of their

income. Such workers usually do not have the savings opportunities such as payroll deductions for deposits into 401(k) retirement plans. Designating a portion of a substantial tax refund for savings may enable workers to save more than they could by diverting only small amounts of their paychecks to savings. Split refunds also make it easier to participate in asset-building programs such as Individual Development Accounts (IDAs) that require individual savings.

How does this work?

Tax filers direct the IRS on how to split their refund among different accounts, by submitting Form 8888 with their return, providing the name of the financial institution, the filer's account numbers and the institution's routing transit number for direct deposits. The split refund option can be chosen whether the return is filed electronically or mailed, and it can be used with any of the IRS 1040 series of tax return forms, including the 1040-EZ. (Tax filers who want to deposit the entire amount of their refund directly into one account don't need to use this form and will continue to designate the account on the tax return form.)

Outreach resources to promote split refunds

The flexibility of split refunds and the Savings Bond option may enable organizations seeking to build stronger linkages between free tax preparation services and asset-building to develop new services attractive to lower-income taxpayers. For example, many VITA sites now partner with a bank or credit union to help tax filers without a bank account to open a new savings account at the site. In doing so, filers can obtain a refund more quickly by filing electronically and having the IRS deposit the tax refund directly into their account.

Several organizations involved in expanding asset development opportunities for lower-income workers, including the Brookings Institution, the D2D Fund, Inc. ("Doorway to Dreams"), and the New America Foundation, previously urged the IRS to offer the split refund opportunity to tax filers and have advocated for the Savings Bond purchase option. Pilot projects with community agencies providing free tax preparation assistance that showed that low-income taxpayers often would respond to the opportunity to save when offered the flexibility of split refunds. For example, one-fifth of VITA clients accepted the opportunity to use split refunds in a pilot conducted by the Community Action Project of Tulsa County in Tulsa, OK, and deposited nearly half the amount of their refunds into savings. Over three-fourths of these workers had no savings previously.

Proponents of the split refund option actively try to increase taxpayer awareness of this opportunity. The D2D Fund, in conjunction with the United Way of America and the National Community Tax Coalition, offers a free "Guide to Split Refunds" which can be ordered at the website www.splitrefunds.net. The Guide provides approaches on how Tax Credit Outreach Campaigns and VITA programs can market saving through split refunds at tax time, how to modify VITA site operations and training to build in the split refund process and how to build financial institution relationships and select savings products appropriate for lower-income workers. The website provides updates on IRS forms and procedures, tax filing software issues and examples of innovative local programs offering split refund opportunities. Also see D2D's website on the new option to purchase Savings Bond, www.d2dfund.org/taxtimebonds.