

# Experts Urge Caution as State Tax Agencies Deploy Generative AI

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Will taxpayers face penalties for relying on bad advice provided by tax departments using generative artificial intelligence?

Experts say it's an important question for the California Department of Tax and Fee Administration (CDTFA) and other state tax departments to consider as they roll out generative AI.

A CDTFA spokesperson told *Tax Notes* August 25 that it launched its generative AI solution, designed to improve the timing and accuracy of answers to taxpayer queries, on August 22.

The CDTFA said that the department has begun logging customer service agents into the new solution and that the tool has already been used by agents in customer service interactions with taxpayers.

Academics and attorneys are concerned that customer service agents using generative AI solutions for taxpayer queries might miss errors in its outputs and provide the incorrect information to taxpayers. Responses from the CDTFA suggest that taxpayers can only challenge incorrect information provided by generative AI if the advice was given in writing.

Pete Sepp of the National Taxpayers Union and Caroline Bruckner, a tax professor at American University's Kogod School of Business and managing director of the Kogod Tax Policy Center, both said it's important for the department to address whether taxpayers will be held responsible if the solution generates an inaccurate response that isn't caught by employees.

"At the end of the day, it's the taxpayer that's signing that tax return that's going to be held accountable," Bruckner said. "That's really important to think through in deploying an AI system."

## Among the First

The CDTFA's AI system will generate responses that pull from the department's reference materials, such as publications, law guides, or material found on its website. A customer service agent will decide when a response is appropriate, the department said.

The CDTFA's system would be among the first and most ambitious generative AI use cases in a state tax department, according to Sepp.

Victoria Noble of the Electronic Frontier Foundation, a nonprofit that advocates for digital civil liberties, called the CDTFA's generative AI an "extremely high-risk use case."

Generative AI tools “are not foolproof” and can “sometimes output incorrect information, which could have serious consequences for taxpayers who rely on bad advice and then make mistakes that expose themselves to tax penalties as a result,” Noble said.

Other states are also deploying generative AI. The Missouri Department of Revenue [announced in](#) June that it implemented generative AI features in its online chatbot, which allows users to “submit more complex inquiries and experience broader response capabilities.”

## ‘Documented Material’

The CDTFA is responsible for collecting the state’s sales and use taxes, along with various fuel, tobacco, and cannabis taxes.

“You can imagine with 42 tax and fee programs, the laws that apply to these different programs . . . can be very complex and difficult to research sometimes,” Thor Dunn, the CDTFA’s customer service chief, told *Tax Notes* August 6. He said the new AI solution, which generates answers from the department’s guidance material and sources, will help customer service agents answer taxpayer questions.

But CDTFA agents aren’t required to use the solution, Dunn stressed. They can ask another agent for information or search through the CDTFA’s reference material manually. The generative AI will reference the statute or publication that it pulls the information from, he added.

The CDTFA told *Tax Notes* that the information compiled by the generative AI will be reviewed by a call center team member before it’s shared verbally with a taxpayer, but taxpayers won’t receive responses in writing.

The department’s [Publication 70](#), which explains taxpayer rights, says that taxpayers who rely on written advice that’s later found to be in error are “excused from paying tax liabilities, including penalties and interest, that are directly related to the erroneous advice.”

But it says that protection doesn’t extend to taxpayers that rely on verbal advice, like those that would be provided by a customer service agent using the generative AI solution, because only “documented material can be used as evidence for erroneous advice.”

Publication 70 encourages taxpayers to contact the Taxpayers’ Rights Advocate Office if they can’t resolve issues through normal channels.

Alfred Buck, the CDTFA’s new taxpayers’ rights advocate and small business liaison, said in a statement to *Tax Notes* that if a taxpayer receives inaccurate information — whether or not the generative AI solution was involved — the Taxpayers’ Rights Advocate Office “helps them navigate their way to a resolution.”

Buck said this will include an independent review of the case, facilitating communication between the taxpayer and CDTFA and advocating for policy or legislative changes.

"Looking forward, we expect fewer inaccuracies as our customer service center agents use the [generative] AI tool to improve the accuracy and quality of the guidance they are already providing," Buck said.

Sepp said the CDTFA's response leaves taxpayers with the same options they had before.

"They can try to seek a written opinion from CDTFA through the conventional request process (which is possible but can take a lot of time), they can take their chances with the verbal guidance they get, or they can contact the Taxpayers' Rights Advocate," he said.

Sepp said the advocate office does a good job with the resources it has but added that he wonders "how many taxpayers will know to get in touch with them over an issue like advice received through generative AI."

## Background

California Gov. Gavin Newsom (D) [earlier this year announced](#) three new state agency agreements for generative AI, including the AI the CDTFA will use to "swiftly search more than 16,000 pages of reference materials and assist staff in providing responses to taxpayers via telephone and live chat."

Under a \$444,600 [contract with](#) SymSoft Solutions LLC, the CDTFA will use generative AI "to enhance taxpayer services by improving the accuracy of information, wait times, and both the customer and team member experiences," according to a contract obtained by *Tax Notes* through a California Public Records Act request.

Before SymSoft Solutions' contract was approved, the company — and another vendor, Ignyte Group — were awarded \$1 by the CDTFA [in 2024](#) to conduct experimental applications of their solutions in a secure and isolated testing environment, known as a "sandbox."

The accuracy of each solution was a major concern for the CDTFA agents who tested them.

During the testing period, SymSoft Solutions' generative AI program demonstrated the ability to increase its accuracy, according to a [December 2024 report](#) obtained by *Tax Notes*. During the first phase, the accuracy of responses decreased by 6 percent but increased by 4 percent in the second phase.

CDTFA agents testing the solution expressed concern about how newer team members could identify whether the generative AI answers were wrong or incomplete.

"Almost all users felt the GenAI technology should be at least as accurate as a human, while many felt it should be held to a higher standard and be nearly perfect in regard to accuracy," the report said.

## Risks, Taxpayer Protections

The risk of AI systems providing inaccurate tax information was flagged in a [2020 paper](#) published in the *Cornell Law Review*.

The paper examined the IRS's [interactive tax assistant](#), an automated system that provides answers to taxpayers regarding whether they are eligible for certain tax credits or whether a certain income is taxable.

The paper's authors — Joshua D. Blank of the University of California, Irvine School of Law, and Leigh Osofsky of the University of North Carolina at Chapel Hill — argued that the tax assistant program simplifies tax law without highlighting underlying complexities, which could result in the government presenting “the law as simpler than it is, leading to less precise advice and potentially inaccurate legal positions.”

Blank and Osofsky, who spoke about federal agencies' use of AI and chatbots to provide legal guidance during a May 1 [Tax Notes Talk podcast](#), said there should be protections for taxpayers that heed the advice of the IRS's system by waiving penalties for legal noncompliance. They said better oversight of the interactive tax assistant is needed and that the government should review the answers it provides.

Sepp said that as generative AI is implemented, it will be important to consider “off ramps for taxpayers with very complex situations to get the help they need.”

Noble and Annette Nellen, a professor at San José State University, both stressed the importance of human review of a generative AI solution's output.

Noble encouraged agencies to adopt policies “ensuring that humans always carefully review — not simply rubber-stamp — AI responses.” Although those safeguards aren't perfect, “they can help prevent some of the harms that these tools could cause,” she said.

And Nellen said she hopes tax agencies will “state for the benefit of everyone that an AI generated explanation should not be relied on to avoid a penalty unless competently reviewed by a human or published by a tax agency.”