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**DIGITAL GOVERNMENT,
PUBLIC-PRIVATE
PARTNERSHIPS, AND
ADMINISTRATIVE BURDENS:**

THE FREE FILE PROGRAM

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Digital Government, Public-Private Partnerships, and Administrative Burdens: The Free File Program

In April of 2019, Intuit, H&R Block, and other members of the tax preparation industry were on the cusp of a major policy victory: codifying a 16-year public-private partnership with the IRS into law. That partnership provides Free File, which promised to offer free tax preparation and e-filing to tens of millions of Americans. But within the space of a couple of months, the law passed without the Free File language, problems with Free File became subject to intense scrutiny, and the IRS was criticized for lax oversight. Soon after, the largest members of the Free File Alliance left, putting the future of the partnership in doubt.

The Free File public-private partnership connected the technological expertise of the private tax preparation industry with a core, albeit unpopular, government service: tax collection. For the public, it replaced paper returns and trips to the post office with a free and seamless online tax return. But it never met expectations. During its most successful year in 2005, only five million taxpayers used the program. Ten years later, half as many taxpayers used it. By 2020, while 70% of taxpayers were eligible for Free File, just 3% used the service.¹

In one crucial respect, Free File was a success for stakeholders. It stopped the government from considering directly providing its own free tax return filing system. In the early 2000s, the US was prepared to do just that. Government officials envisioned letting tax payers file directly with the IRS without a private middleman. Instead, in exchange for the companies offering free tax preparation services for most Americans, the IRS promised to not develop or offer its own competing income tax prep software.

While the IRS kept its end of the bargain the Free File program allowed the tax preparation industry to capture new potential customers. By 2019, four out of five individuals using tax preparation software were using software created either by Intuit or its smaller rival H&R Block.² Many of the public who believed they were signing up for free returns ended up paying because of manipulative, misleading, and deceptive design techniques embedded in the software. A 2019 Inspector General's report estimated that 14 million taxpayers paid for tax

¹Case study prepared by Donald Moynihan, McCourt School of Public Policy, Georgetown University. Acknowledgments: While this case draws from multiple resources, I relied heavily on the excellent investigative reporting from ProPublica, especially reporters Justin Elliott and Paul Kiel. My thanks for their feedback. Thanks to Ian Goldsmith and Caroline Johnson for research help.

Collins, "Legislative Recommendation #4: Set Goals for Substantially Increasing the Use of the Free File Program by Filing Season 2025 and Replace Free File If Those Goals Are Not Attained."

² Elliott and Kiel, "Inside TurboTax's 20-Year Fight to Stop Americans From Filing Their Taxes for Free."

preparation software that they were eligible to receive for free, generating about \$1 billion in profit for the tax preparation industry.³

The case of Free File addresses a number of issues. It touches on the possibilities of digital government to reduce administrative burdens for the public. The case also raises questions of how public-private partnerships operate, and to whose benefit.

The Burdens of Tax Reporting

The American tax system is burdensome. According to the Office of Information and Regulatory Affairs, which estimates time spent completing federal forms, Americans spent 6 billion hours on tax compliance in 2020, the equivalent of about \$220 billion worth of their time.⁴ The IRS itself estimated that, on average, it would take individual taxpayers 8 hours and cost \$140 to file their taxes in 2021.⁵

Many other countries have adopted a “return-free” tax system, in which the government calculates individuals’ tax burdens and taxpayers rarely file a return.⁶ Calls for something similar have been made by Presidents as different as Reagan and Obama, but has never emerged, partly due to the complexity of the US tax code.⁷ People have turned to the private tax preparation industry to help with that complexity. In 2019, the industry generated around \$10.5 billion in revenue.⁸

The IRS piloted electronic tax return filing with five tax preparation companies as early as 1986. E-filing grew quickly in popularity and by 1990 was being used nationwide to file 4.2 million returns.⁹ Simultaneously, a new player in the tax industry emerged, one who would come to dominate the use of technology-assisted tax preparation. In 1984, ChipSoft Inc. launched TurboTax, which quickly became the leading tax preparation software for individuals and small businesses. TurboTax was acquired by Intuit, the developer of financial accounting software Quicken in 1993.¹⁰ By 2000, Intuit controlled 75% of the e-filing market and received \$379 million in revenue from its tax services division.¹¹

³ Elliott and Kiel, “TurboTax-Maker Intuit Will Leave Free Tax Filing Partnership With IRS.”

⁴ Brady, “Tax Complexity 2021: Compliance Burdens Ease for Third Year Since Tax Reform.”

⁵ US Department of the Treasury, Internal Revenue Service, “1040 and 1040-SR Instructions.”

⁶ “What Is Return-Free Filing and How Would It Work?”

⁷ Greene, “Opposition Blocks Return-Free Tax Filing In U.S.”

⁸ IBISWorld, “Tax Preparation Services in the US - Market Size 2003–2027.”

⁹ Internal Revenue Service Newsroom, “Historical Highlights of the IRS”; “E-File Tax History In the United States. Prepare and EFile.”

¹⁰ MLB.com, “Mike Chipman - General Partner.”

¹¹ Intuit, “Intuit 2000 Ann

The Origins of Free File

The Era of Big Government is Over; The Era of Digital Government Begins

While the Free File program was not introduced until 2003, the context for the program goes back to trends beginning in the 1980s. Reagan's proposal for return-free filing failed, but he led a much more successful anti-tax movement. The push for a smaller government opened the door for a bipartisan embrace of outsourcing and public-private partnerships in the Clinton era, most visibly associated with Clinton's Reinventing Government initiative. Conservative groups such as Americans for Tax Reform pushed not just for lower rates but also for reducing IRS budgets.¹²

At the same time that President Clinton was declaring "the era of big government is over" the potential for digital government was growing. Growth in personal computing technology and the Internet caused governments around the world to invest in using these new technologies to provide government services. The Clinton administration spearheaded many e-government initiatives such as promoting e-commerce, requiring all cabinet offices to develop websites, and creating "single point-of-entry" sites that allowed users to easily find government services.¹³ This included interest in expanding e-filing and restructuring the culture of the IRS to be more customer-oriented. E-government initiatives continued into the Bush Administration, with President Bush later signing the E-Government Act of 2002 in order to provide more funding for Internet and electronic government initiatives.¹⁴

The private sector also saw an opportunity in using technology to improve access to government services. In 1999, Intuit launched TurboTax as an online product, bringing in millions of new customers. At around the same time, Intuit began to invest more aggressively in protecting its growing market. It hired former AT&T lobbyist Bernard McKay as its vice president of corporate affairs. McKay was known for his aggressive lobbying style and set to work pushing back against what Intuit saw as government encroachment on their territory.

After a wave of critical reports about overzealous IRS agents, President Clinton signed into law the Restructuring and Reform Act of 1998 (RRA). This legislation expanded taxpayer protections but also set a target of making 80% of all tax returns electronic by 2007. Further, the law required the IRS to "cooperate with and encourage" the private sector in promoting electronic filing, a provision included at the behest of Intuit.¹⁵ At around the same time, Intuit

¹² Burke and Mok, "Trends in the Internal Revenue Service's Funding and Enforcement."

¹³ Clinton, "Memorandum for the Heads of Executive Departments and Agencies on Electronic Government."

¹⁴ Associated Press, "Bush Puts More 'E' in Government"; Frank, "Bush Wants Fast Start on E-Gov"; Turner, E-Government Act of 2002.

¹⁵ Archer, Internal Revenue Service Restructuring and Reform Act of 1998.

began offering free tax preparation for those who made under \$20,000, reportedly as a way to stave off potential government encroachment into its tax filing service.¹⁶

President Bush would also promote digital government. His 2001 *The President's Management Agenda* promoted "Expanded Electronic Government" to "champion citizen-centered electronic government that will result in a major improvement in the federal government's value to the citizen."¹⁷ In response, the Office of Management and Budget (OMB) created a task force, known as "Quicksilver," with the goal of choosing a set of e-government initiatives to fund in line with President Bush's goal. One of the programs chosen was the EZ Tax Filing Initiative, which proposed that the IRS create its own free, automated tax filing software and promote e-filing in line with RRA 1998's goal.¹⁸ According to Mark Forman, who at the time was leading the Quicksilver task force as the OMB Associate Director for IT and E-Government, this proposal "was seen as a low-cost, high-payoff initiative."¹⁹

A Public Service or a Public-Private Partnership?

In 2001 the federal government seemed poised to encourage e-filing by having the IRS directly deliver this program to the public. However, problems began to emerge. In December, a group of eight Republican House Representatives wrote a letter to the head of OMB arguing the EZ Tax Filing Initiative violated OMB's Circular A-76. A-76 is decades-old directive that encourages agencies to rely on the private sector for commercial services. The Bush administration itself enthusiastically used A-76 to encourage contracting out of public services.

Was tax filing a commercial operation? The Republican House members stated that "income tax preparation software and interactive online preparation is well-established non-governmental commercial activity" and that they found "no compelling reason for the federal government to compete in this field." The group was led by Representative Randy "Duke" Cunningham (R-CA), whose district was home to Intuit's headquarters.²⁰

On the other hand, the collection of taxes is an inherently public function, one which private tax preparation services depend on. At the time, taxpayers had to work with a private tax preparer if they wanted to file electronically. OMB documents outlined the value to the public of free e-filing software: "Citizens will no longer have to pay for basic, automated tax preparation.

¹⁶ Hogan, "File Your 1999 Taxes Online"; Elliott and Kiel, "Inside TurboTax's 20-Year Fight to Stop Americans From Filing Their Taxes for Free."

¹⁷ Bush, "The President's Management Agenda."

¹⁸ Forman, "E-Government Strategy: Implementing the President's Management Agenda for E-Government."

¹⁹ Elliott and Kiel, "Inside TurboTax's 20-Year Fight to Stop Americans From Filing Their Taxes for Free."

²⁰ Crenshaw, "IRS Told Its Efforts May Step on Toes Of Private Industry." Cunningham would later resign from Congress and go to prison and tax evasion charges.

Refund checks will be delivered sooner, online security will be increased and customer service will be improved.”²¹

According to Terry Lutes, the IRS’s Director of Electronic Filing, the letter from the eight members of Congress caused “all hell [to break] loose” at the IRS. Staff grew concerned that the EZ Tax Filing Initiative would become a political liability used to attack an agency that was already in the crosshairs. IRS Commissioner Charles Rossotti doubted that Congress would provide enough customer service staff to respond to an increase in questions from online users.²² Rossotti’s concerns were not misplaced. The prevailing small government ethos saw the number of IRS employees drop from 116,673 employees in 1992 to just over 98,000 employees when the RRA was signed in 1998. The decline would continue. In 2010, the IRS had 94,711 employees, dropping to 75,773 employees by 2020. At the same time the IRS had to serve more people with fewer staff – as shown in Figure 1, the US population grew by 28% between 1992 and 2020 even as IRS staff dropped by 35% – and to manage increasingly complex tasks, such as playing a role in the implementation of the Affordable Care Act.²³

²¹ Forman, “E-Government Strategy: Implementing the President’s Management Agenda for E-Government,” 26.

²² Elliott and Kiel, “Inside TurboTax’s 20-Year Fight to Stop Americans From Filing Their Taxes for Free.”

²³ Calculations made by author based on <https://www.irs.gov/statistics/irs-budget-and-workforce>, “Table 31.”

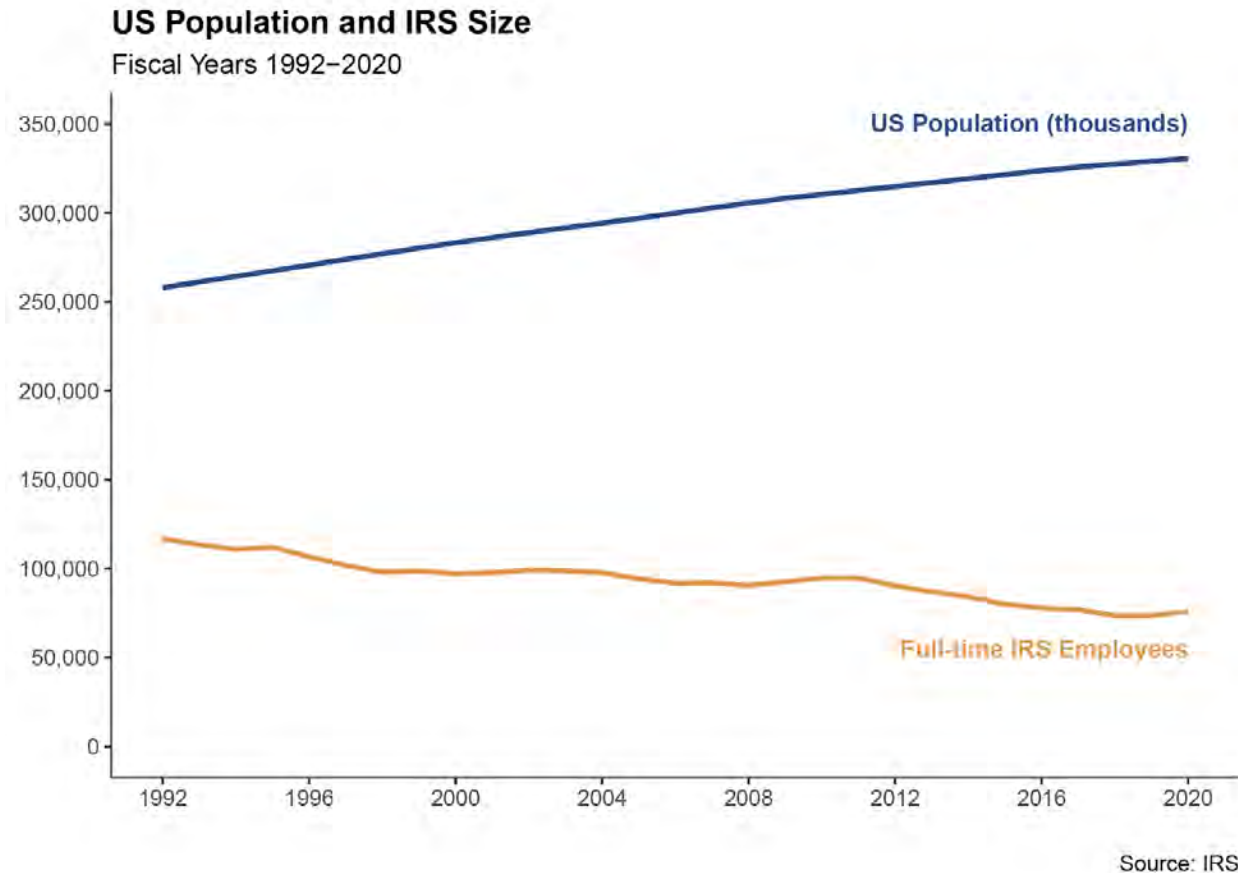


Figure 1

Given declining resources, political demands to expand e-filing, and an aggressive lobbying operation, the IRS saw partnering with Intuit and other private companies as a solution. In January 2002, Treasury Secretary Paul O’Neill formally asked Charles Rossotti to establish a partnership between the IRS and private tax preparation companies to develop a system for helping low-income taxpayers file for free.²⁴ In response, Intuit, H&R Block, and a set of much smaller tax preparation companies formed a coalition called the Free File Alliance and began to negotiate with the IRS.²⁵

After months of negotiations, the IRS and the Free File Alliance signed a “memorandum of understanding” (MOU) on October 30, 2002, establishing the Free File program. The MOU held that, in exchange for the Free File Alliance offering free federal tax services that would cover at least 60% of American taxpayers, the IRS would “not compete with the Consortium in providing free, on-line tax return preparation and filing services to taxpayers.” While Free File

²⁴ Guenther, “The Internal Revenue Service’s Free File Program (FFP): Current Status and Policy Issues.”

²⁵ Elliott and Kiel, “Inside TurboTax’s 20-Year Fight to Stop Americans From Filing Their Taxes for Free.”

would never come close to the 60% target, the IRS kept its pledge not to develop their own product.

Each member of the Alliance was only required to individually cover a minimum of 10% of taxpayers, allowing them to limit Free File provision based on certain characteristics such as age, income, or state. They were also given flexibility on marketing and other services. Additionally, Free File Alliance members were allowed to charge for any services beyond federal tax filing (including state income tax filing or other products) and only required to list their Free File services on a single IRS-owned website.²⁶

Early Success and Tensions

The Free File program was first implemented in 2003, with 2.7 million taxpayers using the service.²⁷ In 2004, one Free File Alliance member named TaxACT decided that they could differentiate themselves by offering Free File services with no restrictions. The CEO, Lance Dunn, saw a marketing value in simplicity: “Why not just make the offer that’s simpler to understand, free for everyone.”²⁸ This approach contrasted with TurboTax’s restrictions that year, which restricted Free File offerings to those “eligible for EIC [Earned Income Credit], [who] are age 22 or younger, age 62 or older, or active Military with a W2.”

In 2005, other members of the Free File Alliance, including Intuit and H&R Block, matched TaxACT’s offer to allow all taxpayers to use Free File. This led to over five million people using the Free File service in 2005, 7.8% of all e-filed returns. By 2018, this number dropped to 2%.²⁹

Spurred by the competition of TaxAct, 2005 would ultimately be Free File’s most successful year. Intuit responded by pushing for further restrictions on Free File offerings. TaxACT CEO Lance Dunn accused Intuit of asking other Free File Alliance members to collude to limit their products, a potential violation of antitrust law.³⁰ The Department of Justice told the IRS that such collusion would likely be considered price fixing. However, the IRS could itself implement restrictions on Free File services.³¹

The public-private partnership of Free File had evolved to a point where the dominant private players were calling on the government to add regulations that restricted competition, to the disadvantage of smaller members of the Alliance and members of the public who would benefit

²⁶ “IRS’ Intent To Enter Into an Agreement With Free File Alliance, LLC (i.e., Free File Alliance).”

²⁷ Internal Revenue Service, Media Relations Office, “IRS SETS NEW TAX FILING SEASON RECORDS.”

²⁸ “United States v. H&R Block, Inc., et al. : Transcript of Preliminary Injunction Hearing - Day 3.”

²⁹ Elliott and Kiel, “Inside TurboTax’s 20-Year Fight to Stop Americans From Filing Their Taxes for Free.”

³⁰ Ibid.

³¹ Hesse to Larson, “Re: IRS Free File Program,” May 9, 2005.

from competition. During a House Committee meeting in April 2005, Intuit CEO Brad Smith stated that the “Free File program has drifted far from its original purpose,” with the original intent being to assist the “the working poor, disadvantaged, and underserved.” Free File had “become a ‘universal-free’ program, operating off a national marketing and sales platform hosted by the IRS,” said Smith, raising concerns about “government serving as either the market-maker for commercial business in this country, or permitting public assets and endorsement to be used for commercial marketing and sales purposes.”³²

In October 2005, the IRS and the Free File Alliance extended the Free File program under a new MOU. Under the new agreement, Free File services would be limited to the lowest 70% of taxpayers based on income.³³ Free File would still be theoretically accessible to more than 90 million households, but strategies like TaxAct’s aggressive marketing were now prohibited. As a result, members of the Free File Alliance could now impose restrictions that made using Free File onerous. The IRS Director of Electronic Tax Administration confirmed that these limits were introduced in response to industry concerns that continued universal Free File service would threaten the future revenues and profits of participating companies.³⁴ In short, Intuit’s arguments had won the day.

Intuit continued to flex its lobbying muscles. A bipartisan Senate proposal to require the IRS to provide free e-filing portal was ultimately never voted on.³⁵ Beginning in 2005, California piloted ReadyReturn, a state return-free filing program aimed at residents with the simplest tax returns. The program was successful and elements were adopted into the statewide tax system. But IRS commissioner Mark Everson (2003-2007) cited the intensity of Intuit’s lobbying against ReadyReturn to explain his doubts about a direct IRS e-filing platform: “there is a big industry out there and they will go to war when this policy is pursued.”³⁶

Troubled Implementation

From Free File to “Free-to-Fee”

After 2005, the Free File program saw an immediate drop in use in the 2006 tax season, with over one million fewer returns. This began a long-term trend of decline. By the 2015 tax season, fewer returns were filed using the program than during its first year in 2003.³⁷ By 2017,

³² Smith, 2005 TAX RETURN FILING SEASON AND THE IRS BUDGET FOR FISCAL YEAR 2006.

³³ US Department of the Treasury, Internal Revenue Service, “Free Online Electronic Tax Filing Agreement.”

³⁴ DuMars to Hugo, “Letter from The IRS to the Free File Alliance,” March 30, 2006.

³⁵ Santorum, Telephone Excise Tax Repeal and Taxpayer Protection and Assistance Act of 2006.

³⁶ Kaste, “IRS Urges E-Filing — But by Vendors Only, Please.”

³⁷ MITRE, “Independent Assessment of the Free File Program, Appendix A: The Economics of IRS Free File.”

only around 2.5 million tax returns were filed through Free File, less than half the number filed in 2005.³⁸

But the IRS would present Free File as a partial success. A 2017 IRS report pointed to Free File's success in "generating a free marketplace" for tax filing services. A 2013 study funded by the Free File Alliance argued that Free File had stimulated free tax preparation outside of the Free File program.³⁹ One of the most likely reasons for this decline was the popularization of "free" commercial tax preparation software offered outside of the Free File Alliance. One lesson of Free File is that "free" was a powerful marketing tool, a way to draw users to a specific provider who might ultimately be charged for the service. The MOU with the IRS did nothing to stop vendors from marketing their own "free" services but with greater control of user experience. Intuit pioneered a variety of troubling and manipulative business practices to push consumers who sought a free file option towards paid products. In effect, while Intuit focused on IRS "encroachment," it and other members of the Free File Alliance had cannibalized the idea of free electronic tax returns.

Users who googled "IRS free file taxes" would find ads offering free services from Free File Alliance members. But the top hits would offer the vendor's own "free" version, rather than the one offered via the IRS web page. This was no accident, but instead was the result of hundreds of millions of dollars in advertising, which overwhelmed any attempts by the IRS to promote Free File on its website. Intuit and H&R Block's Free File pages also included code that made them harder to find in web searches.⁴⁰

If the customer selected the version not from the IRS website, vendor software would put them on a track that would actually charge them, even if they qualified for the free service. TurboTax marketed free services to the military, but then charged those who would have qualified under the Free File version.⁴¹ Deep within the TurboTax FAQ's, users were told that the only way they could get truly free services was by going to the IRS website rather than using the service that Intuit that aggressively marketed as free (Figure 2).⁴² Vendors could also upsell by creating confusion in the mind of users, and offering ancillary products such as loans tied to the taxpayer's refund. Free File Alliance members also marketed their "free-to-fee" products for users who had used their Free File product in the previous year, with the bonus that they retained the user's information to make this year's return easier.⁴³

³⁸ US Department of the Treasury, Treasury Inspector General for Tax Administration, "Results of the 2018 Filing Season."

³⁹ Elliott and Kiel, "Inside TurboTax's 20-Year Fight to Stop Americans From Filing Their Taxes for Free."

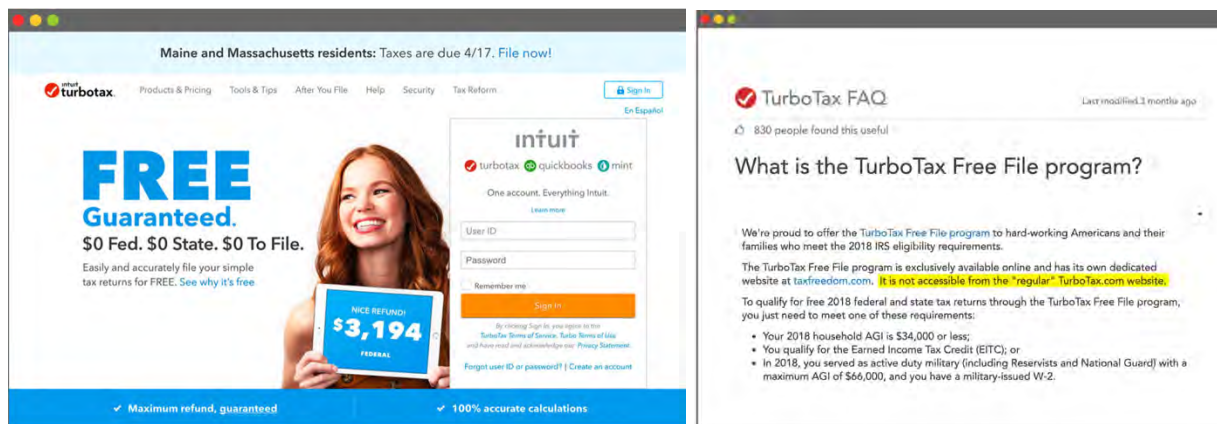
⁴⁰ Elliott, "TurboTax Deliberately Hid Its Free File Page From Search Engines."

⁴¹ Elliot and Tsutsumi, "TurboTax Uses A 'Military Discount' to Trick Troops Into Paying to File Their Taxes."

⁴² Elliot and Waldron, "Here's How TurboTax Just Tricked You Into Paying to File Your Taxes."

⁴³ Ventry, "The Failed Free File Program Should Be Reformed, Not Codified."

Intuit designed its free options such that if a user would ultimately need a paid service, the paywall would not appear until the return was mostly completed, leading many to simply pay the fee rather than find another product. Intuit also created an array of products with highly similar names in order to confuse customers into inadvertently picking paid options. Finding the actual free product that private vendors had agreed to government to provide became akin to finding a needle in a haystack.



Source: Elliot and Waldron 2019

Figure 2

Another reason the Free File program struggled was that the product was simply not very good. Internal IRS data showed many users giving up when trying to find and use the product. Most of the software options had age restrictions, meaning older users had limited options. There were not Free File options for English as a second language. Users frequently experienced errors. Saving the form was complex.

But such concerns were not discussed publicly, and the decline in users was not seen as a source of concern among IRS leadership. The IRS stopped spending money on outreach for Free File after 2014 in order to “save money and be more efficient.”⁴⁴ It also halted producing customer satisfaction surveys, despite only half of users returning from previous years, again citing budget constraints.⁴⁵ By 2018, the National Taxpayer Advocate warned that the Free File program did “not meet the needs and preferences of eligible taxpayers, undermining taxpayers’ *rights to quality service and to pay no more than the correct amount of tax.*” Thus, as members of the Free File Alliance innovated and aggressively marketed their “free” offerings, the actual Free File products remained stagnant.

⁴⁴ Senate Committee on Homeland Security and Governmental Affairs, “IRS Oversight of the Free File Program

⁴⁵ National Taxpayer Advocate, 2018 Annual Report to Congress

Fighting Encroachment

Intuit's ongoing lobbying reflected concerns about IRS "encroachment" that would threaten their business. Lobbying efforts included "mobiliz[ing] and expand[ing] [their] existing coalition" in the media by activating prominent business, policy, and anti-tax movement leaders to publish op-eds defending the Free File program and arguing against return-free filing. Intuit reached out to leaders and nonprofits in minority communities, pursuing a similar op-ed strategy and building partnerships with groups like Women in Public Policy, The Latino Coalition, and the National Black Chamber of Commerce.⁴⁶ For example, a leader of the Asian Business Association wrote an op-ed after a lobbyist provide him with a draft (Figure 3).⁴⁷

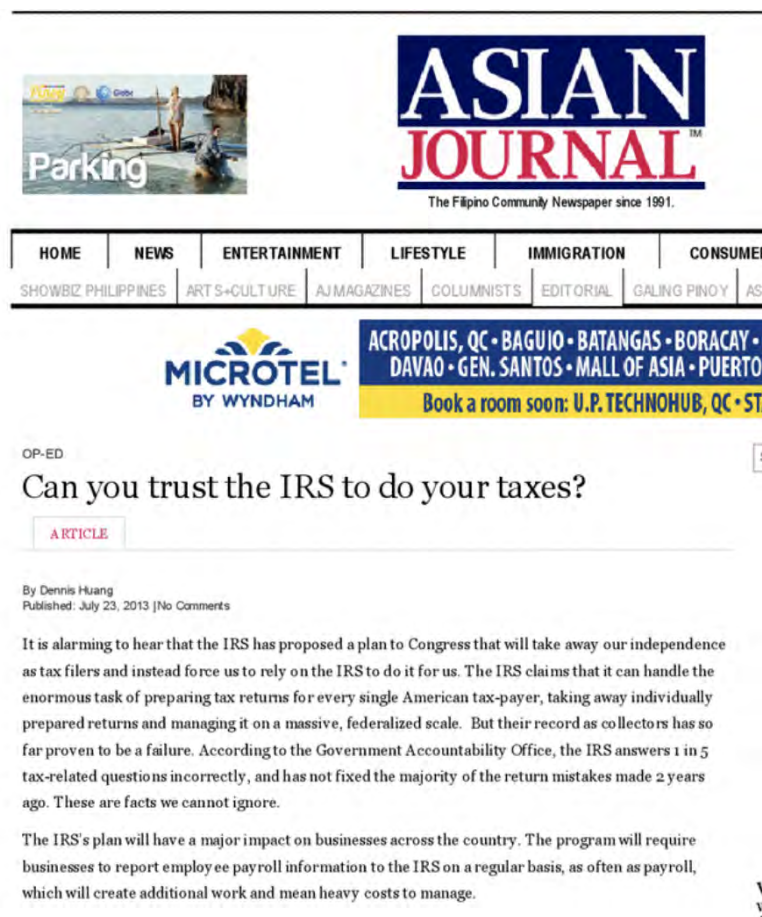


Figure 3

Intuit would also build relationships with IRS officials and use those connections to protect Free File. A former CEO of H&R Block described the IRS Director of Electronic Tax Administration

⁴⁶ Intuit Staff, "FY2014-2015 Encroachment Strategy and Plan Summary"; Day, "TurboTax Maker Linked to 'Grassroots' Campaign Against Free, Simple Tax Filing."

⁴⁷ Day, "TurboTax Maker Linked to 'Grassroots' Campaign Against Free, Simple Tax Filing."

between 2006 and 2010 as “very commercially sensitive” and “particularly open to having sidebar conversations with key people where he could imagine himself landing some day.” In 2018, controversy over an impending advisory board report critical of the Free File program led the IRS to rapidly negotiate a new Free File MOU before the report was published. Correspondence between a Free File Alliance lobbyist and IRS officials at the time pointed to the upcoming 2020 presidential campaign as the reason for an “urgent” renegotiation of the MOU.⁴⁸

Critics of Free File also drew attention from Intuit. One, Dennis Ventry, served as a chair of the critical outside advisory group. Members of the Free File Alliance used California open records laws to compel his employer, University of California-Davis, to turn over anything Professor Ventry had written or said about the companies, which included not just emails but voicemails or text messages. “They are trying to bully me. More importantly, they are trying to chill my research and scholarship,” said Ventry.⁴⁹

The focus on Ventry occurred after he wrote an op-ed opposing what had been a long-term goal of Intuit: codifying Free File into law. Intuit and other members of Free File Alliance had poured millions into lobbying, but efforts to make Free File permanent fell short in 2008, 2013, and 2017. In 2019, the Taxpayer First Act seemed set to deliver their long-pursued goal. Couched within a broader tax bill was language from the Free File Permanence Act of 2017 that would have mandated the IRS’s continued participation in the Free File program. The bill enjoyed bipartisan support and was expected to easily pass the House and Senate.

The Collapse of Free File

Legislative Failure

In April of 2019, on the verge of their goal of making Free File permanent, Intuit and other companies watched as it all fell apart. On April 9th, the day the Taxpayer First bill was scheduled to be voted on in the House, the investigative news outlet ProPublica published a story titled “Congress Is About to Ban the Government from Offering Free Online Tax Filing. Thank TurboTax.” The story highlighted not just the effect of tying the hands of the IRS from providing its own tax filing software, it also centered on the lobbying efforts by members of the Free File Alliance.⁵⁰

⁴⁸ Elliott and Kiel, “Inside TurboTax’s 20-Year Fight to Stop Americans From Filing Their Taxes for Free.”

⁴⁹ Williamson, “Industries Turn Freedom of Information Requests on Their Critics.”

⁵⁰ Elliott, “Congress Is About to Ban the Government From Offering Free Online Tax Filing. Thank TurboTax.”

Reaction to the article was swift. Several progressive lawmakers in the House voiced their opposition to the provision, stating that they were unaware that it was in the bill.⁵¹ The bill passed the House but still needed to pass the Senate. Through the next two months, ProPublica published a steady stream of articles that exposed the problems with Free File, including the deceptive marketing practices by members of the Free File Alliance that seemed to undermine their agreement with the IRS.

The tactics that Intuit and others had used to market “free” tax returns became a source of intense scrutiny. John Lewis (D-GA), who had sponsored the bill in the House, promised to form a working group to study the Free File provision and issues with the partnership.⁵² On May 3rd, a group of 14 Democratic Senators sent a letter to the IRS and the Federal Trade Commission (FTC) asking for an investigation of the program and the tax preparation companies’ business practices.⁵³ On May 6th, the ranking members of the Senate Finance Committee asked the IRS to review problems with Free File, as well as the terms of the MOU.⁵⁴

In the space of a couple of months, the Free File provision in the Taxpayer First legislation had gone from being almost unnoticed to becoming so toxic that Senate leaders decided they could not pass the bill if it remained. By June 14th, the new bill had passed both the House and Senate. It was signed into law by President Trump on July 1st.

New Scrutiny

The scrutiny of Free File did more than stymie a legislative goal of the tax preparation industry. It also brought unwelcome legal attention and led to a broader re-evaluation of the benefits of Free File to both the members of the Alliance and the government. Multiple state attorneys general opened investigations. The New York Department of Financial Services began an investigation into Intuit, H&R Block, and two other companies involved in the Free File program on May 10th,⁵⁵ while the Los Angeles City Attorney filed suit against Intuit for deceiving low-income customers.⁵⁶

The IRS review of the program, released in 2019, confirmed the core criticisms that it was difficult to access Free File and that Free File members used deceptive practices.⁵⁷ But in other respects, the report was less critical. The IRS had outsourced the review to a long-time

⁵¹ Elliott, “Bill to Limit IRS’ Ability to Offer Free Tax Filing Service Is Getting New Scrutiny.”

⁵² Stein and Bade, “House Backs Bill barring IRS from Offering Free Tax Filing Services.”

⁵³ Elliott and Kiel, “Elizabeth Warren and Other Senators Call for Refunds and Investigations of TurboTax and H&R Block.”

⁵⁴ United States Senate Committee on Finance to Rettig, “IRS Letter Re: Free File,” May 6, 2019.

⁵⁵ Elliott, “New York Regulator Launches Investigation Into TurboTax Maker Intuit and H&R Block.”

⁵⁶ Elliott, “TurboTax Tricked Customers Into Paying to File Taxes. Now Several States Are Investigating It.”

⁵⁷ MITRE, “Independent Assessment of the Free File Program.”

contractor, MITRE, who did not recommend significant changes to the program.⁵⁸ For example, in discussing criticism of IRS oversight of Free File, the report stated: “What this critique overlooks is the fact that the Free File program operates as a public-private partnership and, as such, program oversight is a mutual, collaborative effort with the industry, represented by the Free File Alliance. While there is room for improvement, based on assessment findings, MITRE considers the IRS’s current compliance processes adequate and effective to support the integrity of the program.” The review argued that the IRS governance of Free File “effectively allows the program to fulfill the IRS’s currently articulated program goals” while also acknowledging the IRS had no measurable objectives for Free File.⁵⁹ Ron Wyden, the ranking Democratic member of the Senate Finance Committee, said, “This was not the rigorous review needed to ensure all eligible taxpayers are able to easily access and use Free File.”⁶⁰

Later reports would be more critical of Free File, and the IRS. A February 2020 report from the Treasury Inspector General for Tax Administration estimated that more than 14 million taxpayers eligible for Free File may have paid a fee to e-file in 2019. It was also blunter in its criticism of the IRS: “The IRS does not provide adequate oversight to ensure that the Free File Program is operating as intended and in alignment with the MOU.”⁶¹ A bipartisan June 2020 Senate Investigation came to similar conclusion: “Until recently, the IRS conducted little oversight of the Free File program.”⁶² The IRS had once feared pushing too aggressively against the lobbying power of the tax preparation industry. It was now blamed for being too lax in its oversight. The degree to which this was a result of lack of knowledge as to what Free File members were doing, versus indifference or even support for their approach, was hard to discern.

In response to these criticisms, a revised MOU was unveiled in December 2019. Free File members were forbidden from engaging in techniques to hide their Free File offerings and were required to standardize how such products were presented to minimize confusion. The new MOU also dropped the provision that prevents the IRS from competing with private services.⁶³ The revised MOU did not erase criticism. The National Taxpayer Advocate, part of the IRS,

⁵⁸ Elliott, “IRS-Funded Review Confirms TurboTax Hid Free Filing From Search Engines, but Says There’s No Need for Major Changes.”

⁵⁹ MITRE, “Independent Assessment of the Free File Program.”

⁶⁰ Elliott, “IRS-Funded Review Confirms TurboTax Hid Free Filing From Search Engines, but Says There’s No Need for Major Changes.”

⁶¹ US Department of the Treasury, Treasury Inspector General for Tax Administration, “Complexity and Insufficient Oversight of the Free File Program Result in Low Taxpayer Participation.”

⁶² Senate Committee on Homeland Security and Government Affairs, Staff of the Permanent Subcommittee on Investigations, “Re: IRS Oversight of the Free File Program.”

⁶³ Elliott and Kiel, “IRS Reforms Free File Program, Drops Agreement Not to Compete With TurboTax.”

declared that “from a taxpayer perspective, Free File has largely failed,” while noting that low user satisfaction with the program damaged the reputation of the IRS.⁶⁴

By mid-2020, it became clear that the current version of Free File was failing. On June 18th, H&R Block announced that it would be leaving the Free File program at the end of the 2020 tax season. CEO Jeffrey J. Jones stated that the reasoning behind the move was that “we just think it’s in the best interest of the company to move forward in a different direction.”⁶⁵ The next July, Intuit also announced its departure, saying: “With the Free File program surpassing its founding goals of e-file and free tax preparation, and due to the limitations of the Free File program and conflicting demands from those outside the program, we are not able to continue in the program and deliver all of the benefits that can help consumers make more money, save more, and invest for the future.”⁶⁶ With the absence of the two largest companies in the tax industry, the program’s future became shrouded in doubt.

Conclusion

If the purpose of Free File was to push electronic filing, it might be judged a success. More than 90% of taxpayers filed electronically in the 2020 tax season. Of course, in any case, the trend toward e-filing is likely to have increased. If the goal was to provide free access to e-filing, the program’s record looks less positive. While about 110 million people, or 70% of taxpayers are eligible for free filing, only about four million taxpayers used Free File in 2020. Free File Alliance members could boast that they provided free tax software to 17.7 million users in 2019.⁶⁷ Some users may prefer other alternatives, such as paid or volunteer tax preparation or paper forms. But the gap between those eligible for free e-filing and those availing themselves of it remains vast. Intuit and H&R Block remain the primary beneficiaries, dominating the tax preparation services market.⁶⁸

It is unclear what will happen next for Free File and the promise of free electronic tax filing. Ironically, use of the Free File program began rising after the 2017 tax season. The scrutiny of the program may have helped users to understand how to access Free File. The revised MOU encouraged a 50% increase in use between 2019 and 2020.⁶⁹ Some have called for the IRS to

⁶⁴ Collins, *National Taxpayer Advocate 2021 Purple Book*; Ventry, “The Failed Free File Program Should Be Reformed, Not Codified.”

⁶⁵ Versprille and Bseiso, “IRS’s Free File Partners Moving Forward Without H&R Block.”

⁶⁶ Intuit Blog Team, “Accelerating Technology Innovation to Better Help Consumers Solve Their Most Pressing Financial Problems.”

⁶⁷ Collins, *National Taxpayer Advocate 2021 Purple Book*.

⁶⁸ Perri, “TurboTax Market Share Rises in 2021.”

⁶⁹ Internal Revenue Service Newsroom, “IRS Free File Marks Record Increase; Available through Oct. 15.”

use this opportunity to set clear goals for the program, create their own direct e-filing platform, or even to introduce return-free filing.⁷⁰

⁷⁰ Collins, *National Taxpayer Advocate 2021 Purple Book*; Matthews, “The IRS Has a Big Opportunity to Fix the Way Americans File Taxes”; Appelbaum, “Good Riddance, TurboTax. Americans Need a Real ‘Free File’ Program.”

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