

Participation in the IRS Free File Program

by Jacob Goldin

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Jacob Goldin is an assistant professor of law at Stanford Law School and a research expert at the Treasury Office of Tax Analysis. He is grateful to Joe Bankman and Janet McCubbin for their helpful comments. The views expressed herein are those of the author and do not necessarily reflect the views of the

Treasury Department.

In this article, Goldin presents statistics about participation in the IRS Free File program and explores potential explanations for the low participation rate among taxpayers.

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The Free File program is a partnership between the IRS and a consortium of private tax preparation software providers known as the Free File Alliance. Under the program, taxpayers whose income falls below a threshold (\$64,000 for tax year 2016) can use the software of one of the participating companies to prepare and file their federal income taxes for free. The income threshold is set annually so that 70 percent of taxpayers are eligible to participate.

Even though the program is open to most taxpayers, relatively few actually use it. For tax years 2013-2015, about 2.5 million taxpayers filed their returns through Free File per year. Although 2.5 million taxpayers is a large number in absolute terms, it represented just 1.7 percent of the tax return filing population and 2.5 percent of return filers whose income qualified them to participate.

One reason more taxpayers don't use Free File might be that they prefer in-person assistance from a tax return preparer. However, even considering only filers whose income qualified them for Free File and who prepared their own returns, the average Free File usage rate was only 5.5 percent. Similarly, some taxpayers may choose not to use Free File because they don't want to file their taxes online — they may be uncomfortable using a computer, lack internet access, or have concerns with transmitting personal financial information over the internet. Yet among the set of eligible filers who used software to prepare their returns and who filed electronically, just 7 percent used Free File.

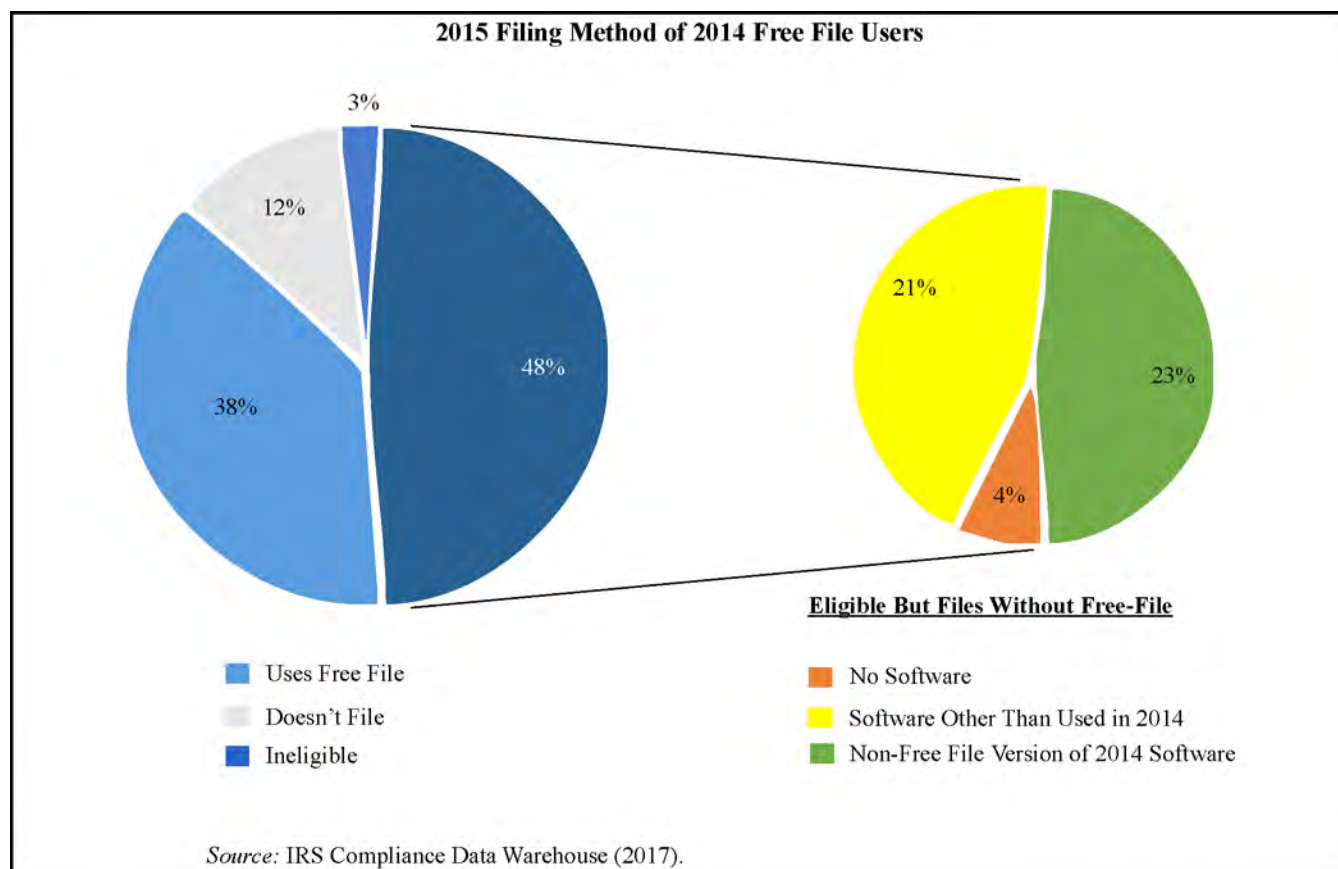
It's likely that a lack of awareness is partially responsible for the low Free File usage rate.¹ Notably, though, even among taxpayers who used Free File to prepare their 2014 tax returns — and who are therefore presumably aware of the program — only 37 percent used Free File again the following year. Some of these 2014 users didn't qualify for Free File in 2015, and others didn't file their 2015 tax returns at all. Yet among those who did file and who did qualify to participate in 2015, less than half (44 percent) used Free File.

The fact that most of the 2014 Free File users didn't use Free File again for 2015 may reflect negative experiences with the Free File program. But the data hint that there is more to the story than that. Of the 2014 users who qualified for Free File in 2015 but who filed using non-Free File software, just over half (52 percent) used the non-Free File version of the same software they had used through Free File in the prior year. This pattern may reflect the common practice of software companies marketing the non-Free File

¹In recent years, cuts to the IRS's budget for marketing Free File have meant that the program has not been widely advertised outside the IRS website.

Free File Participation

| | 2013 | 2014 | 2015 | Average |
|---|-------|-------|-------|---------|
| Total Free File users (thousands) | 2,754 | 2,463 | 2,238 | 2,485 |
| Takeup among: | | | | |
| All filers | 1.9% | 1.7% | 1.5% | 1.7% |
| Eligible filers | 2.8% | 2.5% | 2.2% | 2.5% |
| Eligible, self-preparing filers | 6.3% | 5.5% | 4.8% | 5.5% |
| Eligible, self-preparing, and filing online | 8.2% | 6.9% | 5.9% | 7% |
| Source: IRS Compliance Data Warehouse (2017). | | | | |



versions of their software to taxpayers who filed with them in the prior year through Free File.²

Finally, some taxpayers may have intended to use Free File but inadvertently failed to do so. Using a particular Free File software option requires being eligible for the Free File program as a whole as well

² Taxpayers may not realize the software being advertised to them is not part of the Free File program. For most companies, the non-Free File version of their software is free to some taxpayers who would qualify for Free File but not to others.

as meeting eligibility requirements specific to that software.³ Taxpayers who begin preparing their return using a particular Free File software and later discover they are ineligible for it may continue their return using the non-Free File version. Other taxpayers may mistakenly believe they are using Free File even when they are using non-Free File software from the beginning. For example, as of April 2017, taxpayers who visit freefile.com will find a commercial website presenting information about the Free File program; but if they click the link on that website to begin their return, they will be directed to software owned by the commercial software provider that owns the website, which is free only to a minority of those who would qualify for Free File.⁴ ■

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³These additional restrictions are typically based on age, income, and military status, and sometimes hinge on complicated determinations such as eligibility for the earned income tax credit. See IRS, "Free File Software Offers." Currently, a condition for software providers to participate in Free File is that the Free File version of their software be available to no more than 50 percent of filers.

⁴The freefile.com website contains a small disclaimer stating that it is not endorsed by the IRS or the Free File Alliance, but it is possible that visitors to the site will nonetheless be misled.