

THE IRS DIRECT FILE PROGRAM MISSES THE MARK

With Tax Season Over, It's Clear Direct File is Costly, Confusing and Unnecessary



The nonpartisan Government Accountability Office (GAO) could not substantiate the costs or benefits of the IRS's Direct File program, according to a report the agency released during tax season.

Their findings, combined with Direct File's low adoption rate, raise serious questions about why the Internal Revenue Service (IRS) would expand the program further – when Commissioner Daniel Werfel is already warning of cuts to taxpayer services¹.

In short, the IRS is expanding an expensive, unpopular and redundant program, while reducing its core services. The tax collection agency should not divert vital resources to Direct File, and instead should use this funding to support existing free filing programs and to improve customer service.

“The IRS is struggling with identity theft, backlogs, poor customer service and delayed refunds. How about fixing all that first?”

THE WALL STREET JOURNAL.

¹ | <https://thenationaldesk.com/news/connect-to-congress/irs-commissioner-warns-of-worse-customer-service-lower-tax-collection-if-budget-is-cut-daniel-werfel-treasury-department-inflation-reduction-act-tax-gap-audits>

2024 Direct File in Review



UNDERREPORTED COSTS: The IRS understated the program's cost by failing to include key start-up costs, such as standing up the technology, according to a report from the (GAO). The report noted, **“Without a comprehensive accounting of costs, IRS's estimates could understate the full amount of resources required to develop and maintain a permanent Direct File program.”**²

Bill for Taxpayers: Regardless of the exact cost, Direct File is a new program **funded entirely by the American people**, in contrast to free options, including those offered by private tax preparers, which receive no government funding (see page 3 for more).



QUESTIONS SURROUNDING STATE RETURNS:

Direct File only allows users to prepare their federal returns, compared to commercial tax prep services that handle federal and state returns. It remains unclear how many Direct File users actually completed both their federal and state returns.

Analysis required: The IRS must analyze and share the number of Direct File users who had a state tax-filing obligation and who failed to fulfill that obligation, thereby depriving their state of revenue owed to it.



UNCLEAR BENEFITS: The same GAO report undermined claims from Direct File's supporters about the program's supposed benefits. The GAO could not substantiate claims that Direct File is faster than other tools or leads to increased use of tax credits and deductions.³



LOW ADOPTION: The Administration originally forecasted “several hundred thousand”⁴ taxpayers would prepare and file their taxes through Direct File. In reality, just 140,803 taxpayers — 0.7% of the 19 million eligible Americans in 12 states — used Direct File.

Shifting goal posts: After launching, when the agency saw that goal would be unattainable, it moved the goal posts and now claims that it exceeded its restated goal of 100,000 users.⁵



REDUCED REFUNDS: The average Direct File refund was \$891.78, more than \$2,000 less than the national average.⁶ While some of the gap may be explained by Direct File's limited eligibility, the \$2,000 discrepancy deserves critical analysis by the IRS and assurance that taxpayers are not missing out on credits or deductions for which they are eligible.

Answers needed: The IRS must provide a clear, concise explanation for this disparity. Its answers, so far, have been incomplete, pointing to generalities about those who expect to receive a refund filing before Direct File opened. Further, the IRS has provided no data on the fraud, reject or audit rates of Direct File users.



SCALABILITY UNPROVEN: Expanding Direct File so Americans nationwide, including those with complex returns, can use it will require an enormous investment of both funds and staff hours. Continuous investment will be needed to ensure the software keeps up with changing tax laws.

As former president Obama's Chief Information Officer wrote in The Hill, “Even if completed, [Direct File] will be extremely costly to operate and maintain, and likely would serve as a half-baked and little-used skeleton of already available and fully functional, market-tested commercial software.”⁷

Despite the unquantified costs, unsubstantiated benefits and outstanding questions, the IRS is planning to expand Direct File.

2 | <https://www.gao.gov/products/gao-24-107236>

3 | <https://www.gao.gov/products/gao-24-107236>

4 | <https://www.vox.com/future-perfect/24071005/irs-direct-file-free-tax-software-turbotax-review>

5 | <https://home.treasury.gov/news/press-releases/jy2298#:~:text=WASHINGTON%20E2%80%93%20Today%2C%20the%20U.S.%20Department,ratings%2C%20and%20saved%20taxpayers%20money.>

6 | <https://news.bloombergtax.com/daily-tax-report/free-pilot-costs-fell-below-estimates-at-24-6-million-irs-says>

7 | <https://thehill.com/opinion/4253283-the-governments-free-tax-filing-software-is-virtually-guaranteed-to-fail/>

Other Free Alternatives — Especially Private Ones — Remain Popular

During the 2024 tax-filing season, commercial tax preparers provided more than 26.7 million federal income tax returns at no cost to American taxpayers. The service — worth an estimated \$3.7 billion⁸ — is both a philanthropic effort and a marketing tool.

Private preparers provide exceptional customer service, and free filers are directed to the same resources as paying customers. The easy-to-use tools are available in multiple languages, making them accessible to all Americans.

2023 By the Numbers



Commercial tax preparers provided **25.8 million free federal income tax returns** through their commercial websites (that is, outside of the IRS Free File Program offered at www.irs.gov).⁹



The IRS Free File Program provided another **2.9 million free tax returns**.¹⁰



These figures do not include the many **additional millions of free returns** provided through the government-supported Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs.



The popularity of these programs stands in sharp contrast to Direct File, which drew **just 140,000 users**.

While the IRS provides some funding to VITA and TCE — which is matched by local community partners — the returns completed by private companies and the Free File Alliance come with **no cost to the taxpayer or the federal government**.

Private Options are Popular and Well-Liked

These programs are far more popular than Direct File, despite receiving a fraction of the marketing push the IRS program did. In fact more than 98% of Free File users say they would use it again.¹¹

Expanding Direct File is Costly and Redundant

The more than 30 million free returns completed annually demonstrate there is already an abundance of no-cost options available to taxpayers, while the low adoption rate for Direct File indicates a clear lack of interest in having the IRS serve as tax preparer and collector.

Rather than expanding a redundant and unproven technology, the IRS should redirect its effort to bolstering the Free File program, which provides no-cost returns without leaving taxpayers with the bill.

⁸ | The IRS has stated that the cost on average of preparing a federal income tax return is \$140. No one, of course, is forced to use a commercial tax preparer. But given the complexities of the Internal Revenue Code, millions of Americans choose to do so. This \$3.7 billion figure is derived by multiplying \$140 times the 26.7 million free returns provided by industry in 2024.

⁹ | Internal American Coalition for Taxpayer Rights

¹⁰ | Free File Alliance

¹¹ | Internal Free File Alliance Data

WHAT THE EXPERTS ARE SAYING



It is clear to me that the “free” tax-filing software project (so-called “IRS Direct File”) undertaken by the Department of the Treasury and the Internal Revenue Service is virtually guaranteed to fail.”

Tony Scott,

Federal Chief Information Officer in the Obama Administration.



Many Americans already have access to free tax-prep and filing systems. These include the IRS-run Volunteer Income Tax Assistance program, as well as Free File, a 20-year-old partnership between tax-prep firms and the feds. Big tax-prep outfits also provide free returns for millions of taxpayers. Industry sources estimate that last year more than 28 million Americans filed their returns at zero cost via Free File and free industry offerings. Those services are superior to Direct File in their features, support and technology.”

Wall Street Journal



Direct File is “simply a way to expand the power of the IRS that no one asked for, especially considering Americans already have numerous options for filing free tax returns.”

Rep. Jason Smith,

House Ways and Means Committee Chairman



Direct File has the potential to do more harm than good for taxpayers. It will only enable them to file their federal tax returns. Taxpayers who are unaware that they must separately file state returns will not receive anticipated state refunds this spring. This is significant because many taxpayers who use Direct File are likely to be lower-income and build budgets around anticipated tax refunds. Even worse, confused taxpayers who neglect to file their state returns will be at risk of incurring state penalties.”

Coalition of 18 state tax leaders