

THE TAX FILING SIMPLIFICATION ACT OF 2016

Background

Tax preparation is costly: This tax season, American taxpayers will spend an average of 13 hours preparing their tax returns and will pay about \$200 for tax preparation services – a cost equal to almost 10 percent of the average federal tax refund.¹

The IRS has not implemented mandated reforms: In 1998, a Republican Congress passed an IRS reform bill mandating that the IRS develop procedures to implement a “return-free” tax system to dramatically simplify the filing process for individuals with simple tax situations.² Yet these procedures remain undeveloped nearly a decade after the law’s 2008 implementation deadline. Instead, the IRS has turned over control of the tax filing process to private companies.

The IRS “Free File” program isn’t working for taxpayers:

- The IRS’s Free File program – a partnership between the IRS and private tax software companies – claims to provide free tax preparation services to 70 percent of taxpayers. In reality, only 3 percent of eligible taxpayers use Free File.
- Each software company is allowed to set up its own eligibility criteria, creating a “maze of offerings” that confuses taxpayers into purchasing unnecessary products.³
- Taxpayers wishing to e-file their taxes have no choice but to share sensitive financial information with a private third party – even though a recent audit found that nearly half of Free File companies fail to adequately protect taxpayer data from cybercriminals.⁴
- The National Taxpayer Advocate has consistently called for dismantling Free File.⁵ Instead, the IRS has repeatedly signed binding Free File agreements with the tax preparation industry, pledging that the federal government will “not enter the tax preparation software and e-filing services marketplace.” These agreements block the IRS from offering a free portal that would allow taxpayers to choose to file directly with the federal government.⁶

The Legislation

The Tax Filing Simplification Act of 2016 makes commonsense changes to simplify the tax filing process and lower costs for millions of American taxpayers:

- Prohibits the IRS from entering into agreements that restrict its ability to provide free online tax preparation or filing services.
- Directs the IRS to develop a free, online tax preparation and filing service that would allow all taxpayers to prepare and file their taxes directly with the federal government instead of being forced to share private information with third parties.
- Enhances taxpayer data access by allowing all taxpayers to download third-party-provided tax information that the IRS already has into a software program of their choice.
- Allows eligible taxpayers with simple tax situations to choose a new return-free option, which provides a pre-prepared tax return with income tax liability or refund amount already calculated.
- Mandates that these data and filing options be made available through a secure online function and requires any participating individual to verify his or her identity before accessing tax data.
- Reduces tax fraud by getting third-party income information to the IRS earlier in the tax season, allowing the agency to cross-check this information before issuing refunds.
- This approach to tax filing has been praised in the media and endorsed by tax scholars and a bipartisan set of policymakers.⁷

¹ Internal Revenue Service, “Estimates of Taxpayer Burden” (2015) (online at <https://www.irs.gov/instructions/i1040a/ar03.html>); According to the IRS, the average federal tax refund for the 2016 filing season is \$2,866. IRS, “Filing Season Statistics for Week Ending March 25, 2016” (online at <https://www.irs.gov/uac/Newsroom/Filing-Season-Statistics-for-Week-Ending-March-25-2016>). The \$200 the average American spends on tax preparation services represents 7% of the average refund.

² Sec. 2004 of P.L. 105-206 (105th Congress) (online at <http://www.gpo.gov/fdsys/pkg/PLAW-105publ206/html/PLAW-105publ206.htm>). JCT’s analysis of the 1998 IRS Restructuring and Reform Act states that Section 2004 was adopted because “Congress believed that it could benefit taxpayers to be relieved, to the extent feasible, from the burden of determining tax liability and filing returns. [. . .] The provision requires the Secretary or his delegate to study the feasibility of, and develop procedures for, the implementation of a return-free tax system for appropriate individuals for taxable years beginning after 2007.” JCS-6-98, p. 54-55.

³ Laura Saunders, “Why ‘Free File’ for Taxes Isn’t So Popular: Here’s How to Navigate the Maze of Offerings and Avoid Charges,” *Wall Street Journal* (January 30, 2014) (online at <http://www.wsj.com/articles/why-free-file-for-taxes-isnt-so-popular-1422633546>). *Hearing on Tax Return Preparation Options for Taxpayers: Committee on Finance, United States Senate, 109th Congress* (2006) (statement of Nina E. Olson, National Taxpayer Advocate) (online at https://www.irs.gov/pub/tas/ntatestimonysfc_tax_return_preparation_process040406.pdf).

⁴ Laura Saunders, “Six of 13 IRS-Approved Tax Preparers Fail Cybersecurity Test,” *Wall Street Journal* (February 26, 2016) (online at <http://www.wsj.com/articles/six-of-13-irs-approved-online-tax-prep-services-fail-cybersecurity-test-1456333409>).

⁵ *Hearing on Tax Return Preparation Options for Taxpayers: Committee on Finance, United States Senate, 109th Congress* (2006) (statement of Nina E. Olson, National Taxpayer Advocate) (online at https://www.irs.gov/pub/tas/ntatestimonysfc_tax_return_preparation_process040406.pdf).

⁶ Seventh Memorandum of Understanding on Service Standards and Disputes Between the Internal Revenue Service and Free File, Incorporated (March 6, 2015) (online at https://www.irs.gov/pub/irs-utl/seventh_ff_mou_2015.pdf).

⁷ Farhad Manjoo, “Would You Let the IRS Prepare Your Taxes?” *New York Times* (April 15, 2015) (online at http://www.nytimes.com/2015/04/16/technology/personaltech/turbotax-or-irs-as-tax-preparer-intuit-has-a-favorite.html?_r=1). Dylan Matthews, “Why I’m Boycotting TurboTax This Year,” *Vox* (March 29, 2016) (online at <http://www.vox.com/2016/3/29/11320386/turbotax-boycott-lobbying>). Derek Thompson, “The 10-Second Tax Return,” *The Atlantic* (March 30, 2016) (online at <http://www.theatlantic.com/business/archive/2016/03/the-10-second-tax-return/475899/>). Liz Day, “How the Maker of TurboTax Fought Free, Simple Tax Filing,” *ProPublica* (March 26, 2013) (online at <https://www.propublica.org/article/how-the-maker-of-turbotax-fought-free-simple-tax-filing>). Academic support includes Joseph Bankman (Stanford), “Using Technology to Simplify Individual Tax Filing,” 61 *Nat’l Tax J.* 773 (2008) (online at http://taxprof.typepad.com/taxprof_blog/2009/04/bankman.html). and Dennis Ventry (UC Davis) “Intuit’s Nine Lies Kill State E-Filing Programs and Keep ‘Free’ File Alive,” 57 *STATE TAX NOTES* 555 (2010) (online at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1668912). In May 1985, President Reagan championed a plan under which Americans would “not even have to fill out a return.” Under Reagan’s proposal, Americans would “automatically receive your refund or a letter explaining any additional tax you owe.” President Ronald Reagan, “Address to the Nation on Tax Reform,” speech at the White House, May 29, 1985 (online at <http://www.presidency.ucsb.edu/ws/?pid=38697>). A year later, President Reagan signed the bipartisan Tax Reform Act of 1986 into law, including a provision requiring the IRS to examine the possibility and practicality of implementing return-free filing. Sec. 1582 of P.L. 99-514 (99th Congress).