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# Intuit's Nine Lies Kill State E-Filing Programs and Keep 'Free' File Alive

by Dennis J. Ventry Jr.

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The author thanks Joe Bankman for his helpful comments.

## I. Introduction

Under the auspices of the Free File Alliance (FFA), Intuit, manufacturer of TurboTax, has been attacking state-run, free e-filing services for several years. The latest victim, Virginia's successful iFile program, succumbed late last year.<sup>1</sup> Through it all, the unquestioned crown jewels of state e-filing programs — California's CalFile and ReadyReturn — have managed to survive.<sup>2</sup> But this year, Intuit has ratcheted up its annual campaign to end the two programs. In the process, it is peddling some familiar falsehoods as well as some newly crafted misrepresentations.

This article describes Intuit's nine lies, the false arguments about ReadyReturn and CalFile that

Intuit and its lobbyists have been telling elected officials, staffers, and nonprofit organizations serving California's low-income communities. It also evaluates Intuit's proposed Free File alternative to the state's existing programs. For all of Intuit's assertions — whether regarding the purported shortcomings of the state programs or the purported benefits of the Free File initiative — the article offers a point-by-point refutation.

## II. Tracking Intuit's Lobbying, Loot, and Lies

California offers resident taxpayers two innovative, popular, and free electronic tax filing programs: ReadyReturn and CalFile. Both programs seek to reduce the annual burden and anxiety associated with taxpaying. ReadyReturn provides eligible taxpayers a partially completed state income tax return using wage and income data from a taxpayer's Form W-2 as well as information from prior-year returns. It covers single taxpayers with income up to \$240,000 from wages.<sup>3</sup> Taxpayers can sign and submit their ReadyReturn, make relevant changes before submitting it, use it to fill out a regular return, give it to their accountant, or throw it away. Meanwhile, CalFile offers free online filing for single as well as married taxpayers with somewhat more complicated returns and income up to \$320,000.<sup>4</sup>

Combined, ReadyReturn and CalFile cover 6.4 million Californians, more than 40 percent of all state taxpayers.<sup>5</sup> Annually, they save taxpayers between \$4 million and \$10 million in preparation and filing fees, while also saving the state \$500,000 in reduced processing and administrative costs.<sup>6</sup> Both programs are voluntary. Both use an interview-style

<sup>1</sup>See *infra* notes 14-15 and accompanying text.

<sup>2</sup>Public filings on campaign and committee contributions provide some indication of the importance to Intuit of abolishing California's free e-filing programs. Over the last five years, Intuit spent more than 13 times as much on contributions in California than in all other states combined. For California figures, see Cal-Access, the California secretary of state's website that tracks lobbying activity and campaign contributions, available at <http://cal-access.ss.ca.gov/Campaign/Committees/Detail.aspx?id=1016260&view=contributions>. The data are arranged so that visitors must search by two-year periods and then add the periods to derive total expenditures. This URL does not include data on the \$1 million contribution in 2006 to Tony Strickland, information for which can be found at *infra* note 17. For figures from all other states, see "Follow the Money," sponsored by the National Institute on Money in State Politics (which requires visitors to manually account for contributions to candidates and committees from a larger tabulation of contributions encompassing years 2003-2010), available at <http://www.followthemoney.org/database/topcontributor.phtml?u=3868&y=0&incs=1&ince=1&incf=0&incv=0&so2=T#sorttable2>.

<sup>3</sup>For a full description of the ReadyReturn program, see <http://www.ftb.ca.gov/readyReturn/index.asp>.

<sup>4</sup>For a full description of the CalFile program, see <http://www.ftb.ca.gov/online/calFile/index.asp>.

<sup>5</sup>This and many of the other figures cited in this article were supplied to the author from the California Franchise Tax Board. All of the supporting figures are on file with the author.

<sup>6</sup>*Id.*

format to help users identify favorable income adjustments. And both would disappear if Intuit gets its way.

**ReadyReturn and CalFile save taxpayers between \$4 million and \$10 million annually in preparation and filing fees, while also saving the state \$500,000 in reduced processing and administrative costs.**

For the last five years, Intuit has done everything in its considerable power to kill California's free e-filing programs.<sup>7</sup> The company views the two programs as competition both to its fee-based software (even though ReadyReturn and CalFile users file the simplest returns and have no need for TurboTax) and to Free File, a public-private partnership between the IRS and the FFA, a group of 19 software companies that offer free stripped-down versions of their fee-based software to help some taxpayers file federal returns.<sup>8</sup>

Intuit has spared no expense in its long-running effort to abolish ReadyReturn and CalFile. Since 2005 the company has spent \$1.3 million on lobbyists in California.<sup>9</sup> Over the same period, it contributed an additional \$2.13 million to statewide campaigns,<sup>10</sup> including \$1 million to ReadyReturn foe Tony Strickland during the 2006 state controller's

<sup>7</sup>For representative coverage of these efforts, see *infra* note 13; Dennis J. Ventry Jr., "Intuit Just Won't Quit," *Los Angeles Times* (July 21, 2010), at A17; David Brunori, "Don't Let Intuit Kill ReadyReturn," *State Tax Notes*, Nov. 9, 2009, p. 429 *Doc 2009-24075*, or *2009 STT 214-4*; Dennis J. Ventry Jr., "Intuit Uses Clout to Stymie State Innovation," *The Sacramento Bee* (Oct. 6, 2009), at 11A; Evan Halper, "Defying Legislators, Officials Revive Tax Return Program," *Los Angeles Times* (Dec. 5, 2006), at B1; Tom Campbell, "Who's Opposed to Free Tax Help?" *Los Angeles Times* (May 1, 2006), at B1; Joseph Bankman, "Simple Filing for Average Citizens: The California ReadyReturn," *Tax Notes*, June 13, 2005, p. 1431.

<sup>8</sup>Some members of the Free File Alliance also offer free e-filing of state returns for taxpayers in states that have adopted the Free File model. Other members charge for this service in addition to other "value-added" services. See <http://www.irs.gov/efile/article/0,,id=118986,00.html>. For how FFA providers use deceptive practices in offering those fee-based services to Free File users, see *infra* Falsehood No. 7.

<sup>9</sup>For Intuit's lobbying expenditures between 2005 to the second quarter of 2010, see Cal-Access, available at <http://cal-access.ss.ca.gov/Lobbying/Employers/Detail.aspx?id=1146677&view=activity>. The data are arranged so that visitors must search by two-year periods and then add the periods to derive total lobbying expenditures.

<sup>10</sup>For Intuit's campaign contributions between 2005 and 2010, see Cal-Access, *supra* note 2.

race (Strickland is running for state controller once again this year).<sup>11</sup> Moreover, Intuit has spread its largesse, doling out cash to well over 100 different politicians.<sup>12</sup>

Last year Intuit's efforts resulted in 20 pieces of legislation being held hostage by Senate Republicans during 11th-hour budget negotiations (some of these bills had passed unanimously in the State Assembly). Republican legislators withheld votes in an attempt to do Intuit's bidding and force the abolition of ReadyReturn and CalFile.<sup>13</sup> Ultimately, the state's free tax filing programs survived, but the withheld votes jeopardized funding for domestic violence shelters, police and fire departments, and prevention of swine flu outbreaks.

**Last year Intuit's efforts resulted in 20 pieces of legislation being held hostage by Senate Republicans during 11th-hour budget negotiations.**

This year, with Republicans proven allies, Intuit is targeting Democrats. It has hired lobbyists, including former Democratic staffers and a longtime

<sup>11</sup>See *infra* note 17.

<sup>12</sup>To see which California politicians have received contributions from Intuit since 2005, see either Cal-Access, *supra* note 2 (though it requires adding up recipients year by year) or "Follow the Money," *supra* note 2 (which allows visitors to count up the recipients from 2005 to 2010 in a single table).

<sup>13</sup>See Anthony York, "Turbo Tax Maker Intuit, Again, Is Mired in Political Turmoil," *Capitol Weekly* (Sept. 24, 2009), at A1 ("The late-night breakdown once again brought the software maker Intuit back to center stage in the Capitol melodrama, much to the company's chagrin. While Intuit . . . has largely tried to remain behind the scenes in the state's political battles, their five-year long crusade to eliminate the state's free tax-filing system, Ready Return, essentially brought business in the Capitol to a stand-still."); Shane Goldmacher and Patrick McGreevy, "California GOP Legislators Blocked 20 Bills After Demands Were Unmet," *Los Angeles Times* (Sept. 15, 2009), at A6 ("Republicans in the Senate blocked more than 20 bills . . . to leverage a trio of unrelated demands. Chief among those was the elimination of a program that allowed mostly low-income Californians to have the state do their tax returns free, something the maker of TurboTax has been trying to achieve for years."); George Skelton, "GOP's 'Leverage' Is Tantamount to Extortion," *Los Angeles Times* (Sept. 17, 2009), at A2 (quoting State Treasurer Bill Lockyer (D) as saying, "What's pretty clear now is this: Senate Republicans will abandon domestic violence victims, cops, firefighters and taxpayers to do the bidding of corporate interests."); Evan Halper and Shane Goldmacher, "State Budget Negotiations Were Anything but Smooth," *Los Angeles Times* (July 26, 2009), at A1 (reporting that Intuit approached Democratic leaders about a deal to kill ReadyReturn in July 2009 and that "Republican lawmakers had suggested that if [a deal] happened, they would be more amenable to voting for a key part of the budget plan").

labor representative, to work with members of the majority party. Intuit's pitch to Democrats is for the abolition of ReadyReturn and CalFile in exchange for Intuit helping low-income Californians file state tax returns and claim the federal earned income tax credit through the demonstrably inferior Free File program.

Intuit made the same pitch to Virginia politicians in 2009, with disastrous results for the state's taxpayers. Intuit convinced enough legislators (perhaps by contributing cash to House Speaker William Howell (R) and House Minority Leader Ward Armstrong (D)<sup>14</sup>) to repeal the state's free e-filing service covering nearly every taxpayer, in exchange for adopting the Intuit-backed Free File model covering a fraction of taxpayers.<sup>15</sup>

Of course, Intuit is not the only corporation to use its money to influence legislation and policy. Moreover, as the U.S. Supreme Court held earlier this year,<sup>16</sup> corporate spending on political campaigns amounts to protected speech.

Even if Intuit's efforts to buy votes fail to offend one's sensibilities, its tactics should. And although Intuit's contributions are well-known among state politicians, the company has crafted a lower public profile. Over the years, Intuit has fought its crusade against ReadyReturn and CalFile from the shadows, reluctant to engage in an open discussion on the merits of its campaign. In 2006, for example, Intuit funneled its \$1 million contribution to Strickland through an organization called the Alliance for California's Tomorrow, making the source of the contribution difficult to pinpoint.<sup>17</sup> Moreover, for the last several years, the company has attempted to kill CalFile and ReadyReturn through last-minute deals

while legislators horse-trade during the frenzied waning hours of budget negotiations. The final version of the annual budget bill in California, often given to the full State Legislature with minutes to spare before the state runs out of funding and begins issuing IOUs, is effectively subject to an up-or-down vote. Intuit's strategy not only lacks transparency but also short-circuits the usual processes that subject legislation to hearings, news coverage, and debate. No wonder one veteran California legislator with considerable experience dealing with Intuit (who asked to remain anonymous) reported that the company's reputation in the capitol is at "rock bottom."

Intuit's tactics are on full display in its current attempt to derail ReadyReturn and CalFile. Over the last few weeks, the company has been targeting nonprofit organizations in California that conduct outreach efforts to low-income communities — particularly those serving Latinos, African-Americans, and Asian Pacific Islanders — regarding the virtues of the EITC. The campaign is being run through a public relations firm, which has subcontracted with others to send cover letters to the targeted organizations that contain numerous falsehoods about the state's programs. The cover letters also urge the groups to send an enclosed form letter repeating the falsehoods to each member of California's legislative conference committee.

The letters reveal Intuit's penchant for lying to accomplish its goals. "ReadyReturn is ineffective and a failure," one of the letters asserts. "There were only 54,000 out of 2 million possible ReadyReturn users [in tax year 2009]. That's a 50 percent drop from last year's participation. It's a waste of scarce tax dollars."<sup>18</sup>

Intuit's characterization of ReadyReturn's performance is simply untrue. Indeed, 59,000 taxpayers (not 54,000) filed ReadyReturns for tax year 2009, a year-over-year decline of 2 percent (not 50 percent).<sup>19</sup> Moreover, when combined with CalFile (which jumped 4 percent), participation in the state's free e-filing programs increased by 2 percent

<sup>14</sup>According to the Virginia Public Access Project, Howell received \$30,000 between 2005 and 2009, which was deposited with his political action committee, Dominion Leadership Trust, while Ward received \$5,000 in 2009, which passed through his A Strong Majority PAC. Those figures may seem small compared with Intuit's contributions in California, but they represent nearly one-third of all campaign contributions in Virginia during this period. See [http://www.vpap.org/donors/profile/index/130227?start\\_year=2005&end\\_year=2010&lookup\\_type=year&filing\\_period=all](http://www.vpap.org/donors/profile/index/130227?start_year=2005&end_year=2010&lookup_type=year&filing_period=all).

<sup>15</sup>For coverage of the Virginia legislature's decision to abolish the state's free e-filing program, see Jim Nolan, "State to End Free Online Tax-Filing Service," *Richmond Times-Dispatch* (Apr. 14, 2010), at A-01; and Karen Wilkinson, "Legislation Changes Virginia's Online Tax Preparation Program," *Government Technology* (Apr. 16, 2010), available at [http://www.govtech.com/gt/articles/754091?utm\\_source=rss&utm\\_medium=link](http://www.govtech.com/gt/articles/754091?utm_source=rss&utm_medium=link).

<sup>16</sup>See *Citizens United v. FEC*, 130 S. Ct. 876 (2010).

<sup>17</sup>For Intuit's contribution to the Alliance for California's Tomorrow, see <http://cal-access.ss.ca.gov/Campaign/Committees/Detail.aspx?id=1262979&session=2005&view=received> (visitors must scroll down to view Intuit's \$1 million pledge). For the contribution to Strickland, divided into two payments and made within two days of Intuit's pledge to the Alliance for

(Footnote continued in next column.)

California's Tomorrow, see <http://cal-access.ss.ca.gov/Campaign/Committees/Detail.aspx?id=1262979&view=contribution&session=2005>.

<sup>18</sup>This letter is on file with the author.

<sup>19</sup>*Supra* note 5. ReadyReturn's numbers are even more impressive given that the overall return volume for personal income tax payers in California was down nearly 3 percent in 2009, a decline undoubtedly connected to the flagging economy, which resulted in more taxpayers falling below the filing threshold. Also, the FTB does not now have an advertising budget for the program because Republicans have blocked funding. The FTB has had to use its existing marketing products — including tax booklets, pamphlets, and an annual e-services letter — as well as online social media and traditional media to reach potentially eligible taxpayers.

from 2008 filings.<sup>20</sup> By comparison, participation in the Intuit-backed Free File program fell 9 percent.<sup>21</sup>

The letter goes on to call ReadyReturn “a waste of scarce tax dollars,” while lauding Free File as costing the state of California and taxpayers “nothing.”<sup>22</sup> These, too, are fabrications. ReadyReturn *saved* the state money last year, netting \$30,000.<sup>23</sup> Moreover, Free File is far from free. Substituting Free File for ReadyReturn and CalFile would cost taxpayers between \$4 million and \$10 million in tax preparation fees and the state another \$500,000 in processing and administration.<sup>24</sup> These cost figures do not include deceptive upselling practices that California taxpayers would face under a Free File regime.<sup>25</sup> When taxpayers visit the websites of FFA vendors in an attempt to use the inaptly named Free File service, they face many enticements to purchase “value added” products and “additional services.”

**Participation in the state’s 2009 free e-filing programs increased by 2 percent from 2008 filings, while Free File participation fell by 9 percent.**

Intuit’s false representations — whether contained in the recent letter sent to nonprofits serving California’s poorest communities or in its lobbying efforts to kill ReadyReturn and CalFile while selling Free File to elected officials and policymakers — are legion. The remainder of this article identifies and disproves Intuit’s nine most egregious falsehoods.

**No. 1: ‘Adopting the Free File model in California would cover 70 percent of the state’s taxpayers, considerably more than the state’s existing programs.’** The FFA’s agreement with the IRS requires it to offer service to 70 percent of taxpayers *nationwide*.<sup>26</sup> Currently, that figure corresponds to a national income level of \$57,000. It is not indexed for geographic variation. Thus, in states

with higher per capita income, like California, the \$57,000 threshold covers fewer than 70 percent of taxpayers.

In fact, for Intuit’s claim to be true, the Free File threshold would have to jump 14 percent, from \$57,000 to nearly \$65,000 (based on 2008 tax return data).<sup>27</sup> Currently, the \$57,000 threshold covers just 66 percent of the state’s taxpayers.<sup>28</sup> It is hard to imagine that Intuit fails to understand how Free File’s national index results in varying state-by-state coverage, or that it is ignorant of the program it champions.

Even if California’s per capita income perfectly matched the national data — which it does not — such that 70 percent of California taxpayers had annual incomes less than \$57,000, the agreement between the FFA and the IRS does not require every FFA member to offer service up to that threshold. And in fact, Intuit extends its free service only to taxpayers with incomes up to \$31,000.<sup>29</sup> Despite its restricted coverage, Intuit still captured 41 percent of all FFA volume in tax year 2009, disproportionately more than any other member of the FFA.<sup>30</sup>

In other words, Intuit refuses to serve tens of millions of taxpayers nationwide yet still captures the lion’s share of all Free File traffic (because of its name recognition and dominant market share).<sup>31</sup> Thus, the percentage of taxpayers that effectively would be covered by Intuit’s Free File model would fall still further to somewhere near 50 percent. Indeed, the only way that Free File would cover 70 percent of California taxpayers as Intuit claims

<sup>27</sup>The precise figure corresponding to the 70th percentile of tax filers in California is \$64,793. *Supra* note 5.

<sup>28</sup>*Id.* One might expect the percentage of covered taxpayers under Free File to be even lower given the relative wealth of California residents and the state’s high cost of living. However, California is also home to a large proportion of low- and middle-income taxpayers.

<sup>29</sup>Like all members of the FFA, Intuit offers service to active military with income up to \$57,000. See <http://turbotax.intuit.com/taxfreedom/>. But the number of taxpayers in that group is minimal.

<sup>30</sup>See “Free File, the Intuit Tax Freedom Project, and Intuit Philanthropy,” FTA 2010 E-Filing Symposium (May 2-5, 2010), at 5, slide 9 (the 41 percent figure represents a 5 percent jump from tax year 2008), available at [http://www.taxadmin.org/fta/meet/10fself/pres/Sprouse\\_Intuit\\_FFA.pdf](http://www.taxadmin.org/fta/meet/10fself/pres/Sprouse_Intuit_FFA.pdf).

<sup>31</sup>Intuit’s TurboTax is far and away the number one selling tax preparation software, capturing more than 50 percent of the market in fiscal 2009. Intuit, 2009 Investor Day (Sept. 23, 2009), at slide 94, available at [http://files.shareholder.com/downloads/INTU/751171276x0x320813/19ed991f-0fab-46dc-9380-7bde50da8642/Investor\\_Day\\_2009.pdf](http://files.shareholder.com/downloads/INTU/751171276x0x320813/19ed991f-0fab-46dc-9380-7bde50da8642/Investor_Day_2009.pdf). As further evidence of Intuit’s and TurboTax’s name recognition and dominant market share, nearly 2.18 million California taxpayers (excluding CalFile and ReadyReturn users) e-filed their own returns in tax year 2009 (these taxpayers are known as do-it-yourself filers). Of these DIY filers, 1.59 million (or 73 percent) used TurboTax. *Supra* note 5.

<sup>20</sup>*Id.*

<sup>21</sup>*Id.*

<sup>22</sup>*Supra* note 18.

<sup>23</sup>The FTB estimates that operational costs for the program totaled \$95,000, but reduced processing costs associated with administering ReadyReturn saved the state \$125,000, for a net savings of \$30,000. *Supra* note 5.

<sup>24</sup>*Supra* note 5.

<sup>25</sup>See *infra* Falsehood No. 7 for a detailed discussion of those practices.

<sup>26</sup>See Fifth Memorandum of Understanding on Service Standards and Disputes Between the Internal Revenue Service and Free File Alliance, LLC (Nov. 4, 2009), paras. 1.3 and 1.6 at 3 and article 3 at 5, available at [http://www.irs.gov/pub/irs-utl/signed\\_fifth\\_mou\\_between\\_irs\\_and\\_ffa.pdf](http://www.irs.gov/pub/irs-utl/signed_fifth_mou_between_irs_and_ffa.pdf).

would be if the Free File income threshold were geographically indexed to reflect California's higher per capita income, and all members of the FFA — including Intuit — honored the higher income limit.

**Intuit extends its free service only to taxpayers with incomes up to \$31,000.**

By comparison, ReadyReturn and CalFile, in combination with a number of public-private partnerships coordinated by the state, offer free preparation and e-filing services to nearly every California taxpayer. Recall that ReadyReturn and CalFile cover 6.4 million Californians, more than 40 percent of all the state's taxpayers.<sup>32</sup> Also, the California Franchise Tax Board has entered into formal agreements with seven private e-file providers that offer service for state as well as federal returns to almost the entire remaining taxpaying population.<sup>33</sup>

**No. 2: 'Taxpayers using ReadyReturn pay more in taxes than they should.'** Although repeating it over the years, Intuit has never substantiated its claim — nor is there any evidence in practice — that ReadyReturn overestimates tax liability. Recall that ReadyReturn offers taxpayers a partially completed state tax return using wage and income data already in the state's possession (from a Form W-2, for instance). To the extent the information is incomplete or inaccurate (perhaps the Form W-2 needs to be corrected or the taxpayer acquired an additional dependent during the tax year), the taxpayer can easily update that information online before filing her return.

The only way a taxpayer's estimated ReadyReturn tax liability could be too high would be because of changed household information or circumstances that make itemization desirable. The ReadyReturn program already checks and accounts for those changed circumstances by asking taxpayers relevant questions during the filing process.

Finally, if Intuit's criticism is that a ReadyReturn user will blindly accept her estimated tax liability, that taxpayer is not the kind of person who would be able to complete a tax return on her own or with TurboTax. Indeed, that taxpayer is precisely the person who needs ReadyReturn, a program that assists low- to middle-income taxpayers with uncomplicated returns who may be intimidated by the

filing process and who would be unable or unwilling to fill out a tax return on their own.

**No. 3: 'Neither ReadyReturn nor CalFile helps taxpayers identify adjustments to income, including deductions and credits.'** This is yet another variant of the specious argument that the state-run programs result in taxpayers paying too much tax. Both ReadyReturn and CalFile offer interview or question-and-answer formats that walk taxpayers through their returns, asking them about sources of income and applicable adjustments (CalFile asks more questions than ReadyReturn, because the program serves taxpayers with somewhat more complicated tax situations with additional sources of income and potential adjustments). This format resembles the one used in fee-based software, and helps taxpayers identify tax benefits, including deductions and credits.

It is worth noting that Intuit has been known to use Falsehood No. 3 to insinuate that Free File provides superior service to ReadyReturn and CalFile. The evidence contradicts Intuit's claim. National political leaders on both sides of the aisle have long disparaged Free File. U.S. Sen. Max Baucus, D-Mont., has criticized the program from the beginning,<sup>34</sup> while Sen. Chuck Grassley, R-Iowa, has said that taxpayers would "be better off with a pencil and an abacus."<sup>35</sup> Also, a 2009 study conducted by Tax Analysts revealed that Free File software regularly fails to catch simple mathematical errors and generates disparate refunds for identically situated taxpayers.<sup>36</sup>

**Grassley has said that taxpayers would 'be better off with a pencil and an abacus' than with Free File.**

Moreover, while the Intuit-backed Free File program offers less in terms of technology and service, California works diligently to enhance its free e-filing services. Over the next year, the FTB plans to launch a new e-security platform based on protocols from the financial services sector. The new platform will provide users an even more robust and cutting-edge authentication system, and integrate

<sup>34</sup>Dustin Stamper, "Baucus Concerned New Free File Agreement Is Driving Taxpayers Away," *Tax Notes*, Mar. 20, 2006, p. 1281.

<sup>35</sup>Scott Antonides, "Senate Taxwriters Rebuke IRS on Free File Software Oversight," *Tax Notes*, July 9, 2007, p. 91.

<sup>36</sup>Nicole Duarte, "Tax Analysts Finds Flaws in Free Return Preparation Products," *Tax Notes*, Apr. 20, 2009, p. 286. For additional criticism of Free File, see Asher Hawkins, "Doing Your Taxes, Will Free File Work for You?" *Forbes* (Mar. 18, 2009), available at <http://www.forbes.com/2009/03/18/irs-turbotax-taxcut-personal-finance-taxes-freefile.html>.

<sup>32</sup>*Supra* note 5.

<sup>33</sup>These seven providers operate under a memorandum of agreement that entitles them to be listed prominently on the FTB website as offering free, electronic tax filing services for both state and federal returns. See <http://www.ftb.ca.gov/individuals/efile/allsoftware.shtml>.

the state's suite of e-services so that taxpayers can easily manage their tax accounts online. The project is part of the FTB's broad and innovative taxpayer modernization project whose goal is to provide taxpayers electronic access in a single service to all of their tax account folders (that is, returns, refunds, deficiencies, notices, contacts).

**No. 4: 'Taxpayers using ReadyReturn cannot correct or update information the state uses to populate their return.'** As noted in Falsehood No. 2, a taxpayer can easily correct and update the information on a ReadyReturn such that she receives the full tax benefit of, say, having a child during the tax year or incurring rental payments that make her eligible to receive the state renter's credit. In fact, ReadyReturn's online filing system prompts taxpayers to make those changes to ensure they receive every tax benefit to which they are entitled, asking explicitly, for instance, whether the taxpayer has a child or qualifying dependent, needs "to add or remove a dependent," or paid rent on a primary residence in California for at least half the year.

Reports from various sources indicate that Intuit has been using the example of a low-income, single mother when peddling Falsehood nos. 2-4. In one version of the story, the single mom relies on ReadyReturn to file her state tax return. In so doing, she "misses out" on state child-care credits for expenses associated with the care of her new baby because the state's sources of information do not automatically alert the state to either the new baby or the child-care expenses (such items do not appear on a taxpayer's Form W-2).

Intuit's story reveals its brazenness in misrepresenting ReadyReturn. As explained above, the mom can easily alert the state about her new child. Also, during the filing process, ReadyReturn asks the taxpayer whether she paid someone to care for her child so she "could work or look for work." After updating her ReadyReturn, the new mother's tax liability would be reduced to reflect both the qualifying child and associated child-care expenses.

**No. 5: 'The state's free tax filing services hurt low-income taxpayers by ignoring the earned income tax credit, a federal tax subsidy for the working poor.'** First, this criticism is misplaced. Ready Return and CalFile assist resident taxpayers in filing state returns. The EITC is a federal credit that taxpayers can claim only on federal returns. Criticizing the state for not having a line on its personal income tax forms dedicated to claiming a subsidy run entirely by a federal agency would be like criticizing the IRS for not including a line on its Form 1040 for claiming California's renter's credit.

As importantly, simply filing a state tax return will never secure a federal EITC payment for a California taxpayer. Recognizing that reality, the state makes numerous and monumental efforts to alert all potentially eligible EITC claimants residing in California. For years, the FTB has collaborated with the IRS in a joint marketing program to target eligible recipients of the credit. Also, the FTB prominently displays information pertaining to the EITC on multiple pages on its website, in FTB tax booklets and pamphlets, and in its e-services mailings. Each of those outreach efforts educates taxpayers on the program's qualifying criteria and how to claim the credit. The state has also teamed with a number of private software companies to assist eligible Californians in claiming the credit through the FTB website.<sup>37</sup> That collaboration is part of a more encompassing agreement between the state and participating companies to provide California taxpayers free e-filing services for federal returns. And although Intuit has refused to participate in this public-private partnership, five other members of the FFA offer free e-filing services to Californians through the program. Finally, since 2008, every state employer has been required to notify employees of their potential eligibility for the EITC.<sup>38</sup>

In its recent campaign targeting nonprofit organizations serving California's low-income communities, Intuit has implied that the state is to blame for more than \$1 billion in unclaimed EITC benefits for resident taxpayers. Intuit's charge not only ignores the intense outreach efforts described above but also reveals the company's ignorance of the relationship between the federal credit and potential claimants. As described in more detail below, the vast majority of unclaimed EITC claimants do not file a state tax return because their income falls below the state's filing threshold. No change in California's filing programs will secure those residents a federal credit.

In 2009 the IRS mailed over 75,000 notices to Californians who had filed a 2007 federal return without claiming the EITC, but who, based on IRS data, may have qualified for the credit.<sup>39</sup> Less than 30 percent of that filing population responded to the letter.<sup>40</sup> Importantly, that filing population is different from the larger population of Californians — over 700,000 residents — who do not have a filing

<sup>37</sup>See <http://www.ftb.ca.gov/individuals/efile/allsoftware.shtml>.

<sup>38</sup>See [http://www.edd.ca.gov/Payroll\\_Taxes/pdf/EarnedIncomeTaxCredit.pdf](http://www.edd.ca.gov/Payroll_Taxes/pdf/EarnedIncomeTaxCredit.pdf) and [http://www.edd.ca.gov/Payroll\\_Taxes/FAQ\\_-\\_Earned\\_Income\\_Tax\\_Credit\\_Notification.htm](http://www.edd.ca.gov/Payroll_Taxes/FAQ_-_Earned_Income_Tax_Credit_Notification.htm).

<sup>39</sup>*Supra* note 5.

<sup>40</sup>*Id.*

requirement in the first place (largely because their income falls below the filing threshold) but who may still qualify for the EITC.<sup>41</sup> California's outreach programs described above target both populations of potentially eligible EITC claimants, while Intuit's Free File does not. Also, those Californians who file a ReadyReturn or use CalFile are directed by the state programs to federal filing sites that ensure they get the EITC they deserve. In the end, the underclaim rate that continues to plague the EITC has considerably more to do with the ineffectiveness of Free File than with the purported shortcomings of the state's truly free e-filing programs.

**No. 6: 'Intuit's Free File would provide a service that Californians do not enjoy under ReadyReturn or CalFile.'** Intuit has linked this falsehood to Falsehood No. 5 in its attempt to demonstrate that substituting Free File for ReadyReturn and CalFile would benefit California taxpayers. But Intuit's Free File offers nothing that California does not already have. In fact, far from helping California, the only thing Intuit's Free File would provide state residents is reduced coverage, inferior service, and millions of dollars in out-of-pocket expenses for tax preparation and filing.

*Reduced Coverage From Free File.* As described in Falsehood No. 1, California has already arranged to offer almost every resident taxpayer free e-filing services for both state and federal returns.<sup>42</sup> ReadyReturn and CalFile cover slightly more than 40 percent of all taxpayers, while the state's public-private partnerships with software vendors cover the remaining population of taxpayers. By comparison, Intuit's Free File alternative would offer free e-filing services to, at most, 66 percent of Californians, while leaving the other 34 percent of resident taxpayers to fend for themselves with fee-based services.<sup>43</sup>

*Inferior Service From Free File.* As discussed in Falsehood No. 3, the Free File program has faced withering criticism for years from national leaders for failing to provide taxpayers with user-friendly and reliable software. Also, independent studies have confirmed congressional suspicions that FFA vendors have been offering taxpayers inferior software with clunky interfaces, high rates of mathematical errors, and miscalculated refunds. And while FFA members merely provide stripped-down versions of their fee-based software, California's FTB continues to enhance its free e-filing programs, both in terms of service and security, through its innovative, multiyear modernization project.

<sup>41</sup>*Id.* A small percentage of nonfilers in California may in fact have a filing requirement, but they do not submit a return because they have sufficient withholding.

<sup>42</sup>See *supra* notes 32-33 and accompanying text.

<sup>43</sup>See *supra* notes 27-29 and accompanying text.

It is also important to recall the discussion of ReadyReturn and CalFile in Falsehood nos. 2-5. These programs already offer all the functionality and services (and then some) of Intuit's proposed Free File. ReadyReturn and CalFile allow taxpayers to update their tax information to reflect changes from previous years, assist taxpayers in identifying changed tax circumstances and income adjustments, and reach out to all potentially eligible EITC claimants in California.

*Higher Costs From Free File.* For California taxpayers, a world without ReadyReturn and CalFile would create significantly higher costs associated with tax filing. As already noted, the two programs save taxpayers millions of dollars each year in filing expenses,<sup>44</sup> while also saving the state an estimated half-million dollars in processing and administrative costs.<sup>45</sup> Add to these costs those associated with the deceptive upselling practices used by Free File providers. These practices are described in Falsehood No. 7.

**No. 7: 'Free File would cost California taxpayers and the state nothing.'** As should be clear, Intuit's Free File plan is far from free. In addition to raising filing costs for taxpayers and administrative costs for tax officials, Free File would expose Californians to the unregulated practice among Free File providers of upselling fee-based products.<sup>46</sup> Taxpayers visit Free File with the reasonable expectation of receiving free e-filing assistance. But the FFA's agreement with the IRS requires it to offer free preparation and e-filing services for federal returns to only 70 percent of the national tax filing population; for all other services, members can charge taxpayers whatever they want. Without reliable data or appropriate oversight, the revenue potential for upselling through Free File is limitless.

Thus, while Intuit touts Free File as a free service, it is really a bundled marketing package that offers a loss leader (that is, a free federal return for a restricted number of taxpayers) and fee-based services for nearly everything else (including state tax returns). Only a few of the FFA vendors offer free

<sup>44</sup>*Supra* note 5.

<sup>45</sup>In a Free File world, some percentage of previously covered ReadyReturn and CalFile users would switch from electronic to paper returns, the latter of which cost the state an additional \$2.25 per return to process compared with electronic returns. The actual cost is \$2.59 per paper return versus 34 cents per e-filed return. *Supra* note 5.

<sup>46</sup>Neither the FFA nor the IRS publishes data on how much revenue is generated from fees charged for state preparation services or other "value added" services sold through the inaptly named Free File program. See David R. Williams, director, electronic tax administration and refundable credits, IRS, to Robert Cohen, executive director, Legal Aid Society of Orange County, July 14, 2008, at 1, on file with the author (stating the IRS does not track charges for state returns).



e-filing of state returns, and not for every state. Taxpayers in states where e-filing is not supported must pay a fee to file state returns.

Also, FFA members use unsavory tactics to scare taxpayers into purchasing “value-added” services. Their websites ask visitors “Want more security?” or “Want more value?” with the clear intent of raising doubt in taxpayers’ minds about whether the free services are as secure or as reliable as the fee-based services. Those same tactics produced refund anticipation loans that, until recently, Free File providers featured prominently on their websites.<sup>47</sup> Those predatory lending practices involved the Free File provider advancing taxpayers the value of their expected federal income tax refund while charging exorbitant interest rates.

Given those rapacious practices and the anxiety they create, it should come as no surprise that FFA members generate significant revenue from upselling fee-based products through the Free File interface. Although it is hard to determine with any precision how much FFA providers generate from upselling — because the FFA refuses to report such statistics, and the IRS, inexplicably, feels no responsibility to regulate the practice — there is reason to believe that Intuit made as much as \$25 million in upselling through the Free File program in tax year 2008.<sup>48</sup>

Intuit’s participation in the FFA is motivated neither by altruism nor by a desire to make taxpaying less expensive for the lower-income taxpayers the program was designed to serve. Rather, Intuit views Free File explicitly as a source of revenue. Abolishing state-run programs like Ready Return and CalFile while swapping in Free File would generate considerable revenue for Intuit in at least three ways.

<sup>47</sup>See, e.g., Dustin Stamper, “Free File Alliance Agrees to Stop Peddling Extra Services,” *Tax Notes*, Dec. 11, 2006, p. 966; Dustin Stamper, “Free File Not Free Enough for Top Taxwriter,” *Tax Notes*, Apr. 24, 2006, p. 418.

<sup>48</sup>That estimate is based on a slide contained in Intuit’s 2009 Investor Day presentation to shareholders. See *supra* note 31, at slide 92 (reporting \$25 million in revenue from “Free Federal EF decision”). There is no way to verify whether the figure reflects, understates, or overstates the actual upselling revenue Intuit generated from Free File, because Intuit refuses to disclose such figures in a comprehensible fashion and the IRS turns a blind eye to upselling practices. It is possible that the \$25 million reference in Intuit’s presentation relates to something else altogether. Intuit recently stopped charging a separate fee to customers for e-filing a completed return (for which it also charged a fee). By not charging that fee (and presumably collapsing the two fees into a single fee), Intuit may have increased customer usage of its products and thus revenue (which, in the presentation, it may be attributing to dropping the fee). However, without an explanation from Intuit, the available information could just as easily be interpreted as reflecting revenue from upselling.

First, as the Microsoft Windows of tax preparation software, Intuit’s TurboTax would further entrench its dominant market position. Given the name recognition of TurboTax, new Free File customers would more likely choose Intuit than any of the other 21 Free File providers. In fact, Intuit already captures more Free File volume than any FFA member, even though its Free File offerings cover only taxpayers with income up to \$31,000 (not \$57,000, like other FFA members).<sup>49</sup>

Second, and as described above, Free File offers Intuit significant upselling opportunities. The only thing Intuit offers for free through Free File is the most basic stripped-down software for the least sophisticated federal returns and for state returns in only 21 states. All other services are fee based, including state returns not served by Intuit and “value added” services that promise “bigger tax savings,” “maximizing” deductions and refunds, and delivering “the full value of donations.”<sup>50</sup> Based on the face value of those advertisements, a visitor to Intuit’s Free File website might reasonably ask whether using the free product will result in a higher tax bill, fewer deductions, a lower refund, and lost value for charitable contributions.

Finally, Intuit’s business model views Free File as a “free-to-fee” service. In particular, it conceptualizes its participation in Free File as a way to further entrench itself as the leader in fee-based tax preparation software by transitioning nonpaying or partially paying customers to its fee-based products (because those taxpayers start reporting income beyond Free File’s income threshold, their returns get too complicated for the stripped-down Free File software, they question the reliability of the crude interface and reduced capabilities of Free File, or they fall victim to Intuit’s upselling techniques). In its 2009 Investor Day presentation, Intuit explicitly acknowledged its free-to-fee strategy by laying out its “Free Works” philosophy in a series of slides captioned, “Free Works . . . Gaining Share,” “Free Works . . . Adding Customers,” and “Free Works . . . Strong Margins.”<sup>51</sup>

Finally, it is worth noting that the agreement negotiated between the FFA and the IRS prohibits any member of the FFA from offering strictly free services. That is an odd prohibition given the FFA’s stated mission to provide lower-income Americans tax filing services “all online” and “all free.”<sup>52</sup>

Consider the experience of the Legal Aid Society of Orange County (LASOC), which offers free e-filing

<sup>49</sup>See *supra* Falsehood No. 1 for a fuller discussion.

<sup>50</sup>See <http://turbotax.intuit.com/taxfreedom/>.

<sup>51</sup>See *supra* note 31, at slides 94, 95, and 97.

<sup>52</sup>See <http://www.freefilealliance.org/>.

through its website, I-CAN! E-File.<sup>53</sup> When LASOC initially sought membership in the FFA, Intuit and other FFA members fought the effort because LASOC wanted to offer all its services for free. LASOC expressed surprise about that conflict because, as it said in correspondence with the IRS, the program, was called “Free File.”<sup>54</sup> With the threat of litigation looming and after granting LASOC’s Freedom of Information Act request for communications between the FFA and IRS pertaining to LASOC, the IRS agreed to list the organization on its website as a Free File provider (for which it pays a fee), but it prevented LASOC from offering free services that compete with the FFA’s fee-based services. Meanwhile, the FFA continued to refuse membership to LASOC, a position that explains why there are 19 official members of the FFA but 20 e-filing vendors listed on the IRS Free File website, including non-member I-CAN! E-File.

**No. 8: ‘Intuit’s Free File alternative would simplify filing for California taxpayers.’**

Abandoning CalFile and ReadyReturn in favor of Intuit’s Free File would complicate rather than simplify tax filing for Californians. For one thing, nothing is simpler than ReadyReturn, which provides taxpayers a completed and always correctable tax return. Replacing ReadyReturn with a fill-in state return (as Intuit proposes) would increase the filing burden on taxpayers and eliminate a popular program that by all accounts lowers the annual anxiety that accompanies tax season.<sup>55</sup> Also, CalFile users would save, at most, a few keystrokes under a Free File program that electronically transferred tax information from a state to a federal return. The time saved in electronically versus manually importing basic information such as adjusted gross income, number of dependents, or filing status is insignificant for the simple returns filed under the state’s programs, and it certainly does not form a sufficient basis to support a claim of broad-based simplification.

<sup>53</sup>See <http://www.icanefile.org/?caller=711>. On a shoestring budget, LASOC’s I-CAN! E-File initiative assists a remarkable number of taxpayers each year. For tax year 2009, for instance, it helped taxpayers file nearly 84,000 returns, while securing \$144 million in total refunds and \$44 million in EITC payments.

<sup>54</sup>Robert Cohen, executive director, Legal Aid Society of Orange County to David R. Williams, director, electronic tax administration and refundable credits, IRS, Apr. 15, 2008, at 2, on file with the author (noting, “While in fact in some limited instances, it is possible to obtain tax services from providers listed under ‘freefile’ that are free, more often federal tax services for which there is no charge are offered in conjunction with state tax services for which there is a charge. . . . In other words, I would guess that many, if not the vast majority of users of the ‘freefile’ website, are in fact charged for services.”).

<sup>55</sup>See *infra* note 58 and accompanying text.

As part of its false argument that Free File offers magic simplification features, Intuit has asserted that its alternative to the state’s programs would save taxpayers the trouble of “doing their taxes twice.”<sup>56</sup> Unless Intuit convinces both the IRS and every applicable state to abandon their respective income tax forms in favor of a universal form, taxpayers will always have to “do their taxes twice.” That complication is unavoidable under a federal system of government and the reality of multiple taxing jurisdictions.

Finally, if Intuit is arguing that Free File would make tax filing easier because it would fill in returns based on information the company has in its possession from returns filed in previous years, or from what the taxpayer told the company through its electronic interface, that is exactly what ReadyReturn and CalFile already do, albeit more cheaply and effectively.

**No. 9: ‘California’s ReadyReturn program creates a conflict of interest whereby the state both prepares and audits a taxpayer’s return.’**

That falsehood, while certainly provocative, is a red herring. Regardless of whether a taxpayer uses ReadyReturn or CalFile or a paid preparer or Free File, the state is already in possession of all the tax account information it would or could use to assist a taxpayer in filing her taxes. To the extent the state enters that information onto a tax return and sends it to the taxpayer, the state — as the ultimate auditor of that return — is giving the taxpayer a chance to see what it knows well before it ever decides to audit the return. That transparency is simply honest customer service, and something taxpayers appreciate about the program.

**User satisfaction with the ReadyReturn program exceeds 98 percent and is a testament to the program’s success.**

California is hardly in the business of preparing resident tax returns. Indeed, preparers traditionally assist their clients by interpreting tax laws, weighing the likelihood of success of various tax positions, and laying out alternative reporting scenarios. California does no such thing. Its prefilling work does not

<sup>56</sup>See letter to the editor, “The View From Intuit,” *Los Angeles Times* (July 21, 2010) (responding to an op-ed criticizing Intuit, and repeating many of the falsehoods described in this article), available at <http://www.latimes.com/news/opinion/letters/la-le-0804-wednesday-20100804,0,2067230.story?page=3>.

include opining on the tax laws or considering alternative outcomes for sophisticated tax positions. Its clients have simple returns, and they benefit from the simplest assistance.

The state is more scrivener than preparer when it prepopulates a ReadyReturn. Before sending out a taxpayer's ReadyReturn, California takes information the taxpayer has already provided and attested to — either on a prior year's tax return or her federal Form W-2 — and inputs that information for the taxpayer onto a state tax return. That process amounts to nothing more than data entry.

The state's simple, transparent service saves taxpayers time.<sup>57</sup> It also eases the inevitable anxiety associated with paying one's taxes. It lets taxpayers know what the state knows, which is only what taxpayers or third parties have already reported. And it makes the state seem less like an impersonal leviathan and more like a partner. User satisfaction with the ReadyReturn program (the prepopulated return, the cutting-edge and user-friendly electronic interface, and the efficient service) exceeds 98 percent and is a testament to the program's success: "Great service . . . takes the stress out of taxes!"; "LOVE, LOVE, LOVE this service"; "THIS IS THE BEST SERVICE I HAVE EVER SEEN BY THE GOVERNMENT"; and "this system rocks!"<sup>58</sup>

Finally, as part of Falsehood No. 9, Intuit representatives have gone on record as saying that in no other system "are you allowed to be both the preparer and the auditor."<sup>59</sup> Once again, Intuit is wrong. In fact, such a system perfectly describes Free File. Through its agreement with the FFA, the federal government deputizes a select number of software companies, advertises their names on the IRS website, and encourages taxpayers to consider

selecting one of the companies to assist in preparing and filing federal tax returns that may be subject to future IRS examination, audit, and challenge.

### III. Conclusion

Despite Intuit's well-funded campaign of disinformation designed to kill California's free e-filing services, CalFile and ReadyReturn continue to offer resident taxpayers free, innovative, secure, and popular e-filing services. In fact, in combination with private-sector partners, California offers nearly every resident free e-filing services for state as well as federal returns. The best Intuit's Free File model can offer is service for only two-thirds of California taxpayers, and probably no more than one half given the company's disproportionate share of all Free File volume and its denial of service to tens of millions of taxpayers otherwise eligible for the Free File program.<sup>60</sup> In addition to covering almost twice as many taxpayers as Intuit's Free File model, California's free e-filing services save taxpayers and the state money, while offering higher-quality service and capabilities, eschewing predatory upselling practices, and reaching out to the entire population of potential EITC claimants.

As policymakers consider ways to ease the anxiety and burden associated with taxpaying, particularly for low- and middle-income Americans, they should certainly debate the merits of providing e-filing services through private versus public efforts or some combination of the two. Intuit refuses to engage in such a debate, preferring instead to operate in the shadows, and to persuade legislators with money, hired guns, and falsehoods. It is clear that Intuit is not interested in participating in public-private partnerships that serve the public interest. Nor is it interested in protecting the "free" in Free File. Rather, Intuit wants to abolish yet another state-run e-filing program that actually saves taxpayers money, time, and anxiety. After all, a strategy of making taxpaying scary, hard, and complex sells considerably more tax preparation software. ☆

<sup>57</sup>Which is undoubtedly why Intuit opposes the program. California does for free what Intuit charges customers, that is, imports information onto a current-year return from forms W-2 and 1099 and the prior year's return.

<sup>58</sup>These and thousands of other quotations from satisfied customers can be viewed at [http://www.ftb.ca.gov/readyreturn/user\\_fedback.shtml](http://www.ftb.ca.gov/readyreturn/user_fedback.shtml) (listing all user comments in unfiltered fashion). (Last accessed on August 23, 2010.)

<sup>59</sup>John Howard, "Debate Over Online State Tax Filing Heats Up in Capitol," *Capitol Weekly* (July 29, 2010), at A6 (quoting Intuit spokeswoman Whitney MacDougall).

<sup>60</sup>See *supra* notes 26-31 and accompanying text.