



# Free File Demographics and Migration Analysis



# **Free File Demographics and Migration Analysis TY 2008**

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## **Electronic Tax Administration and Refundable Credits**

# Background

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To increase electronic filing, it is imperative that the IRS understand its markets, measure the success of past marketing efforts, and track changes in taxpayer behavior. In an effort to increase the number of individual income tax returns filed electronically, Electronic Tax Administration and Refundable Credits (ETARC) officials have requested an analysis of taxpayers who use the Free File program.

The Free File program is a free federal tax preparation and electronic filing program for eligible taxpayers developed through a partnership between the IRS and the Free File Alliance, a group of private sector tax preparation companies. For processing year (PY) 2009 [tax year (TY) 2008], the Free File program allows taxpayers earning \$56,000 or less to file their federal tax returns for free with no hidden fees, which contributes to overall IRS electronic filing.

# Brief Methodology

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WIRA addressed five research problems in order to better understand Free File taxpayers and to track their behavior. Data was queried through the use of Structured Query Language (SQL) programming. The primary data source was the ETA Marketing Database. WIRA used descriptive statistics and market segmentation to profile various taxpayer populations of interest. Additional analysis was performed to answer specific business questions.

For the migration analysis (Research Problem 5), WIRA analyzed individual taxpayers instead of tax returns. Since a taxpayer could have filed as primary in one year and secondary in another, a taxpayer-based approach allows for a more complete analysis. After the data files were uploaded to CDW and validated, SAS programming was used to query the data sets to answer the business question.

# Tax Filing Type Definitions

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- **Free File:** For TY 2008, consortium indicator present, Online return, no RAL/RAC requested, and adjusted gross income of equal or less than \$56,000 (CONSORTIUM-IND = 'C' or 'S' and TRDBTY08 = '3' and TRDBRAL = '0' and AGICOMP <= 56,000)
- **Spanish Free File:** For TY 2008, consortium indicator present, Online return, no RAL/RAC requested, and adjusted gross income of equal or less than \$56,000 (CONSORTIUM-IND = 'S' and TRDBTY08 = '3' and TRDBRAL = '0' and AGICOMP <= 56,000)
- **Free Fill Fillable Form:** For TY 2008, consortium indicator present (CONSORTIUM-IND = 'F')
- **ELF:** Electronic filing by Paid-Preparer (TRDBTY08 = '1')
- **Online:** Electronic filing by Self-Preparer (TRDBTY08 = '3')
- **V-Code:** V-Code and paper indicators present (PROCCDVIND = '1' and TRDBTY08 = '0')
- **True Paper (not V-Coded):** Paper indicator present and V-Code indicator not present ( TRDBTY08 = '0' and PROCCDVIND not equal to '1')

# *Research Problem 1:*

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**What are the demographic characteristics of the TY 2008 Free Filers? How do their demographics compare to the TY 2007, TY 2006 and TY 2005 Free Filers? What was their filing behavior in TY 2007, TY 2006 and TY 2005? What populations should ETARC target for their Free File marketing efforts?**

# ***TY 2008 Free Filer Volume Decreased by Over 1,750,000***

**Table 1: Number of Free Filers by Tax Year**

	<b>TY 2005</b>	<b>TY 2006</b>	<b>TY 2007</b>	<b>TY 2008</b>
Free Filers	3,783,306	3,854,549	4,768,474	3,009,614*
% Change	-	1.9%	23.7%	(36.9%)

Source: ETA IMF Marketing Database

\* The volume of TY 2008 Free Filers includes Spanish Free Filers

The number of Free Filers decreased significantly from TY 2007 to TY 2008. A major factor is that more software providers offered alternative free federal tax return packages to lure taxpayers in 2008. The existence of the Free File program showed industry that free tax service models attract customers and can, ultimately, generate business profits. As a result, a number of software providers have moved aggressively to offer free products in the commercial space. Free File has driven the creation of a private market of free services -- services that are more broadly marketed than Free File's offerings. That market, in turn, is in direct competition with the Free File program and may well account for the decline in Free File usage.

# TY 2008 Free Filers' Prior Year Filing Behavior

Table 2: Volumes of Different Filing Methods by Tax Year

Filing Methods*	TY 2005	TY 2006	TY 2007
<b>Free File</b>	571,607 (19.0%)	782,711 (26.0%)	1,195,128 (39.7%)
<b>Online (not Free File)</b>	374,441 (12.4%)	431,104 (14.3%)	510,049 (17.0%)
<b>ELF</b>	486,183 (16.2%)	469,772 (15.6%)	409,438 (13.6%)
<b>Paper (not V-Coded)</b>	413,580 (13.7%)	377,135 (12.5%)	281,087 (9.3%)
<b>V-Coded</b>	292,895 (8.7%)	239,639 (8.0%)	190,631 (6.3%)
<b>Not Filed in Respective Year</b>	900,908 (29.9%)	709,253 (23.6%)	423,281 (14.1%)
<b>Total</b> (Total volume of Free Filers in TY 2008)	3,009,614 (100.0%)	3,009,614 (100.0%)	3,009,614 (100.0%)

- Excluding taxpayers who did not file in the previous years, TY 2008 Free Filers are comprised mostly of former Free Filers.
- True paper filers share of of TY 2008 Free Filers has decreased the most from TY 2005 to TY 2007 (4.4 percentage points).
- The volume of taxpayers who did not file decreased by almost 47% between TY 2005 and TY 2007.

# Top Categories of Free Filers TY 2005 to TY 2008

**Table 3: Top Categories of Free Filers by Tax Year**

Top Category	TY 2005	TY 2006	TY 2007	TY 2008
Age - Under 25	41.8%	40.9%	36.7%	35.3%
AGI - \$0 to \$17,000	51.0%	50.4%	53.1%	47.7%
0 Dependents	77.5%	76.2%	76.8%	71.5%
Simple Return Type	62.5%	60.0%	60.8%	53.1%
Filing Status - Single	73.2%	72.0%	71.9%	67.1%
Refund	94.5%	94.8%	86.8%	94.1%
No EITC	77.4%	75.9%	76.1%	71.0%
No Education Tax Credit Claimed	94.0%	93.3%	94.7%	93.9%
No Form 2441 Present	97.2%	96.9%	97.1%	96.6%
No Direct Debit	60.1%	57.9%	59.9%	58.6%
Direct Deposit Accepted	74.5%	76.4%	76.7%	82.2%

- Of the filing attributes that were examined, Table 3 presents the categories with the highest percentage of Free Filers in TY 2005, TY 2006, TY 2007, and TY 2008.
- These categories were examined independently, so the table does not imply all Free Filers fall under all of the categories.
- The top categories are the same every year. Though there are big increases in Refunds and Accepted Direct Deposits from TY 2007 to TY 2008, their volumes actually decreased (4.1 M to 2.8 M and 3.2 M to 2.3 M, respectively).

Source: ETA IMF Marketing Database

# Age of Free Filers

Table 4: Percentage of Free Filers by Age and Tax Year

Age	TY 2005	TY 2006	TY 2007	TY 2008
Under 25	41.8%	40.9%	36.7%	35.3%
25 to 34	28.0%	28.4%	26.6%	28.1%
35 to 44	14.1%	14.3%	14.5%	15.3%
45 to 54	9.7%	9.9%	11.0%	11.9%
55 to 64	4.4%	4.3%	5.3%	5.8%
65 and Over	2.0%	2.2%	6.0%	3.5%
<b>Total</b>	<b>100.0%</b> <b>(3,783,306)</b>	<b>100.0%</b> <b>(3,854,549)</b>	<b>100.0%</b> <b>(4,768,474)</b>	<b>100.0%</b> <b>(3,009,614)</b>

Source: ETA IMF Marketing Database

- Age filing distributions remained fairly consistent over time, with a slight decrease in young taxpayers under 25 years in TY 2007 and older taxpayers 65 years and over in TY 2008.

# Adjusted Gross Income of Free Filers

**Table 5: Percentage of Free Filers by Adjusted Gross Income and Tax Year**

Adjusted Gross Income (AGI)	TY 2005	TY 2006	TY 2007	TY 2008
Negative AGI	0.3%	0.4%	0.4%	0.5%
\$0 to \$17,000	51.0%	50.4%	53.1%	47.7%
\$17,001 to \$25,000	19.0%	18.7%	16.7%	18.5%
\$25,001 to \$35,000	17.0%	16.7%	15.6%	17.1%
\$35,001 to \$50,000	12.7%	12.9%	12.4%	13.4%
\$50,001 to \$75,000	0.0%	0.9%	1.8%	2.8%
\$75,001 to \$100,000	0.0%	0.0%	0.0%	0.0%
\$100,001 or More	0.0%	0.0%	0.0%	0.0%
<b>Total</b>	<b>100.0%</b> <b>(3,783,306)</b>	<b>100.0%</b> <b>(3,854,549)</b>	<b>100.0%</b> <b>(4,768,474)</b>	<b>100.0%</b> <b>(3,009,614)</b>

Source: ETA IMF Marketing Database

- Free Filers with AGI range \$0 to \$17,000 decreased slightly from TY 2007 to TY 2008 (5.4 pts), while those with AGI range \$50,001 to \$75,000 increased slightly in the same tax period (volume also increased slightly over 1,000). Though the percentage of Free Filers in the other AGI ranges increased slightly in the same tax period, their volumes decreased.

# Balance Due/Refund/Even of Free Filers

**Table 6: Percentage of Free Filers by Balance Due/Refund and Tax Year**

Balance Due or Refund	TY 2005	TY 2006	TY 2007	TY 2008
Refund	94.5%	94.8%	86.8%	94.1%
Balance Due	4.4%	4.5%	5.1%	4.1%
Even	1.1%	0.7%	8.1%	1.8%
<b>Total</b>	<b>100.0%</b> <b>(3,783,306)</b>	<b>100.0%</b> <b>(3,854,549)</b>	<b>100.0%</b> <b>(4,768,474)</b>	<b>100.0%</b> <b>(3,009,614)</b>

Source: ETA IMF Marketing Database

- Though Free Filers with refunds increased approximately 7.3 percentage points from TY 2007 to TY 2008, their volume decreased by 1.3 M.
- Even Return proportions returned to their usual levels after the aberration caused by the Economic Stimulus Package offered in TY 2007.

# Volume and Percentage of e-filers, Free File Fillable Form (FFFF) Users, and Total Tax Returns for Three Age Ranges TY 2008

**Table 7: Volume and Percentage of e-filers, FFFF Users, and Total Tax Returns for Three Selected Age Ranges TY 2008**

Taxpayer Age Group	e-file Volume (OL, ELF)	FFFF User Volume	Total Volume of Tax Returns	e-file %* (OL, ELF)	FFFF User %*
Under 25 years	15,529,008	95,819	22,520,255	69.0%	0.4%
25 yrs. – 34 yrs.	21,060,234	64,283	26,511,212	79.4%	0.2%
65 yrs. and over	10,736,498	8,617	19,769,434	54.3%	0.0%

Source: ETA IMF Marketing Database

\* Percentages are based on total volume of tax returns in the respective age ranges.

# Target Populations for TY 2010 Marketing Free File Program

**Table 8: Potential Free Filers by Selected Demographic Groups (TY 2008)**

Taxpayer Group	Potential Free File Volume*	Potential Free File %**
True Paper Filers who Self-Prepared (under 25 years)	2,643,374	11.7%
True Paper Filers who Self-Prepared (25 yrs – 34 yrs.)	1,305,727	4.9%
True Paper Filers who Self-Prepared (65 yrs. and over)	1,768,173	8.9%
V-Coders who Self-Prepared (under 25 years)	1,919,046	8.5%
V-Coders who Self-prepared (25 yrs. – 34 yrs.)	1,244,942	4.7%
V-Coders who Self-Prepared (65 yrs. and over)	1,059,408	5.4%

- Self-Prepared True Paper Filers under 25 years have highest volume and percentage of potential Free Filers.
- Combined True Paper Filers and V-Coders under 25 years who Self-Prepared have higher volume and percentage of potential Free Filers (20.3%) than Senior Citizens 65 years and over who Self-prepared and used True Paper or V-Code filing.

Source: ETA IMF Marketing Database

\* Potential Free Filer identification criteria: AGI =< \$ 56,000 and self-preparing and paper filing.

\*\* Percentages are based on total volume of tax returns in the respective age ranges (see Table 7).

# ***Research Problem 2:***

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**What are the demographic characteristics of the TY 2008 Free File Fillable Form users? What was their filing behavior in TY 2007? What populations should ETARC target for their Free File Fillable Form marketing efforts?**

# ***Top Categories of Free File Fillable Form Users TY 2008***

**Table 9: Top Categories of TY 2008 Free File Fillable Form Users**

<b>Top Category</b>	<b>Volume</b>
Age - Under 25	35.2%
AGI - \$0 to \$17,000	40.9%
Zero Dependents	80.4%
Simple Return Type	60.7%
Filing Status - Single	69.7%
Refund Return	91.9%
No EITC Claimed	90.8%
No Education Tax Credit Claimed	95.5%
No Form 2441 Present	97.4%
Direct Debit	51.9%
Direct Deposit Accepted	82.6%

- Of the filing attributes that were examined, Table 9 presents the categories with the highest percentage of Free File Fillable Form users for TY 2008.
- These categories were examined independently, so the table does not imply Free File Fillable Form users fall under all of the categories.

Source: ETA IMF Marketing Database

# Adjusted Gross Income and Age of Free File Fillable Form Users

**Table 10: Adjusted Gross Income of TY 2008 Free File Fillable Form Users**

Adjusted Gross Income (AGI)	Volume	Percentage
Negative AGI	938	0.3%
\$0 to \$17,000	111,391	40.9%
\$17,001 to \$25,000	28,857	10.6%
\$25,001 to \$35,000	30,368	11.1%
\$35,001 to \$50,000	36,412	13.4%
\$50,001 to \$75,000	34,810	12.8%
\$75,001 to \$100,000	16,668	6.1%
\$100,001 or More	13,156	4.8%
<b>Total</b>	<b>272,600</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

**Table 11: Age of TY 2008 Free File Fillable Form Users**

Age	Volume	Percentage
Under 25	95,819	35.2%
25-34	64,283	23.6%
35-44	40,547	14.9%
45-54	38,756	14.2%
55-64	24,578	9.0%
65 and Over	8,617	3.2%
<b>Total</b>	<b>272,600</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

- 73.7 % of Free File Fillable Form users are 44 years and under.

# Tax Return Complexity and Balance Due/Refund for Free File Fillable Form Users

**Table 12: Tax Return Complexity of TY 2008 Free File Fillable Form Users**

Return Complexity*	Volume	Percentage
Simple	165,547	60.7%
Intermediate	71,003	26.1%
Complex	36,050	13.2%
<b>Total</b>	<b>272,600</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

\*Simple - Form 1040, 1040A, or 1040EZ, without any schedules

Intermediate - Form 1040A with schedules or 1040 with schedules A,B,D, Additional Child Tax Credit, Educational Credits, Child Care Credit, Credit for the Elderly or EIC

Complex - Form 1040 with schedules C,E or F or other schedules and all other specific Forms 1040, e.g. 1040PR, etc.

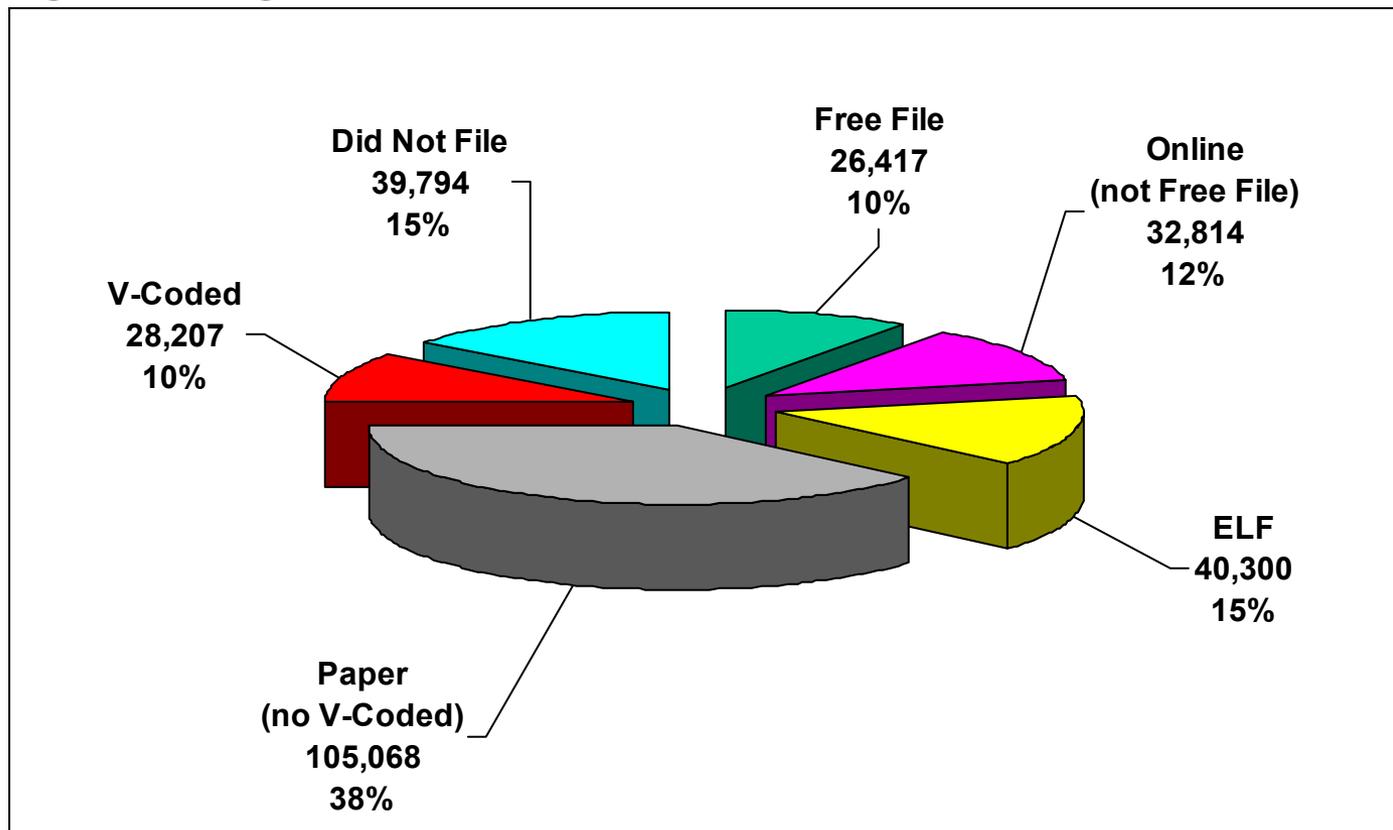
**Table 13: Balance Due/Refund of TY 2008 Free File Fillable Form Users**

Balance Due or Refund	Volume	Percentage
Refund	250,536	91.9%
Balance Due	16,519	6.1%
Even	5,545	2.0%
<b>Total</b>	<b>272,600</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

# TY 2007 Filing Behavior of TY 2008 Free File Fillable Form Users

Figure 1: Filing Method of TY 2008 Free File Fillable Form Users\* in TY 2007



Source: ETA IMF Marketing Database

\* The volume is based on primary SSNs only.

# Target Populations for TY 2010 Marketing Free File Fillable Form Program

**Table 14: Potential Free File Fillable Form (FFFF) Users by Selected Demographic Groups TY 2008**

Taxpayer Group	Potential FFFF User Volume*	Potential FFFF User %**
True Paper Filers who Self-Prepared (under 25 years)	2,657,056	11.8%
True Paper Filers who Self-Prepared (25 yrs – 34 yrs.)	1,533,428	5.8%
True Paper Filers who Self-Prepared (65 yrs. and over)	2,356,130	11.9%
V-Coders who Self-Prepared (under 25 years)	1,940,015	8.6%
V-Coders who Self-prepared (25 yrs. – 34 yrs.)	1,585,501	6.0%
V-Coders who Self-Prepared (65 yrs. and over)	1,533,097	7.8%

- Self-Prepared True Paper Filers under 25 years have highest volume of potential Free Filers compared to senior citizens 65 years and over.
- Combined True Paper Filers and V-Coders under 25 years who Self-Prepared have higher volume of potential Free Filers compared to Senior Citizens 65 years and over who Self-prepared and used True Paper or V-Code filing (a difference of 707,844).
- The different taxpayer groups in this table include the volumes of potential Free Filers with AGI <= \$56,000 for the respective age group and filing method (Table 8).

Source: ETA IMF Marketing Database

\* Potential FFFF User identification criteria: Self-preparing and Paper Filing.

\*\* Percentages are based on total volume of tax returns in the respective age ranges (see Table 7).

# ***Research Problem 3:***

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**What are the demographic characteristics of the TY 2008 Spanish Free File users? What was their filing behavior in TY 2007? Are there any unique demographic characteristics that ETARC might consider for marketing the Spanish Free File program?**

# Top Categories of Spanish Free Filers TY 2008

**Table 15: Top Categories of TY 2008 Spanish Free Filers**

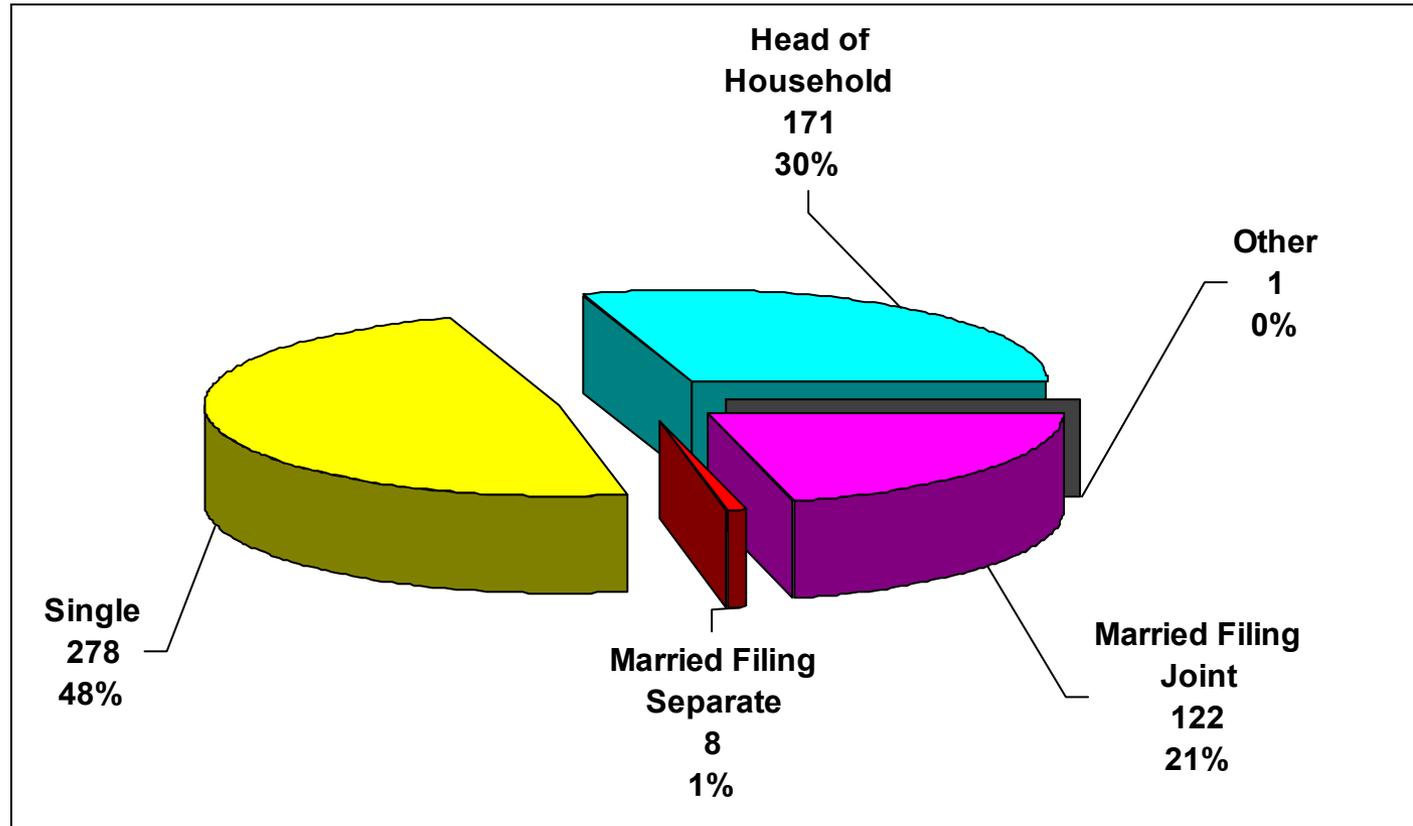
Top Category	Volume
Age – 25 to 34	31.9%
AGI - \$0 to \$17,000	60.9%
Zero Dependents	52.6%
Simple Return Type	51.2%
Filing Status - Single	47.9%
Refund Return	93.3%
No EITC Claimed	60.9%
No Education Tax Credit Claimed	98.5%
No Form 2441 Present	98.1%
Direct Debit	53.9%
Direct Deposit Accepted	82.8%

- Of the filing attributes that were examined, Table 15 presents the categories with the highest percentage of Spanish Free Filers for TY 2008.
- These categories were examined independently, so the table does not imply Spanish Free Filers fall under all of the categories.

Source: ETA IMF Marketing Database

# Filing Status of TY 2008 Spanish Free Filers

Figure 2: Filing Status of TY 2008 Spanish Free Filers



Source: ETA IMF Marketing Database

# Adjusted Gross Income and Age of Spanish Free Filers

**Table 16: Adjusted Gross Income of TY 2008 Spanish Free Filers**

Adjusted Gross Income (AGI)	Volume	Percentage
Negative AGI	1	0.2%
\$0 to \$17,000	353	60.9%
\$17,001 to \$25,000	132	22.8%
\$25,001 to \$35,000	71	12.2%
\$35,001 to \$50,000	22	3.8%
\$50,001 to \$75,000	1	0.2%
\$75,001 to \$100,000	0	0.0%
\$100,001 or More	0	0.0%
<b>Total</b>	<b>580</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

**Table 17: Age of TY 2008 Spanish Free Filers**

Age	Volume	Percentage
Under 25	115	19.8%
25-34	185	31.9%
35-44	145	25.0%
45-54	75	12.9%
55-64	47	8.1%
65 and Over	13	2.2%
<b>Total</b>	<b>580</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

- 76.7 % of Spanish Free Filers are 44 years and under.

# Tax Return Complexity and Balance Due/Refund for Spanish Free Filers

**Table 18: Tax Return Complexity of TY 2008 Spanish Free Filers**

Return Complexity*	Volume	Percentage
Simple	297	51.2%
Intermediate	197	34.0%
Complex	86	14.8%
<b>Total</b>	<b>580</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

\* See slide 17 for Return Complexity category definitions.

**Table 19: Balance Due/Refund of TY 2008 Spanish Free Filers**

Balance Due or Refund	Volume	Percentage
Refund	541	93.3%
Balance Due	26	4.5%
Even	13	2.2%
<b>Total</b>	<b>580</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

- 82.8 percent of Spanish Free Filers who had refunds received their refunds through direct deposit.

# States with Largest Volume of Spanish Free Filers

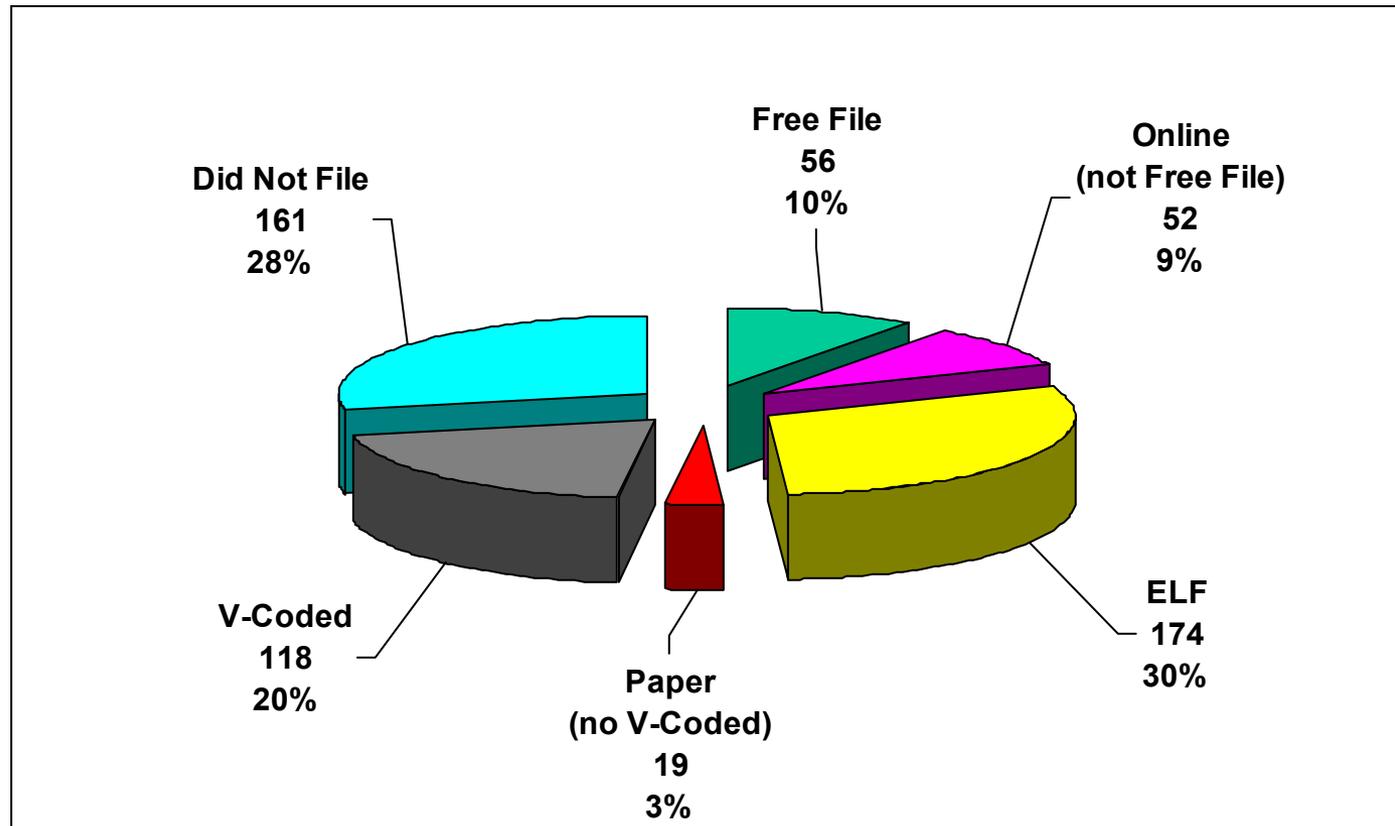
Table 20: Top 6 States for TY 2008 Spanish Free Filers

State	Volume	Percentage
Florida	185	31.9%
California	102	17.6%
Texas	73	12.6%
New York	35	6.0%
New Jersey	19	3.3%
Illinois	18	3.1%
Other	148	25.5%
<b>Total</b>	<b>580</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

# TY 2007 Filing Behavior of TY 2008 Spanish Free Filers

Figure 3: Filing Method of TY 2008 Spanish Free Filers\* in TY 2007



Source: ETA IMF Marketing Database

\* The volume is based on primary SSNs only.

# Marketing For Spanish Free File Program

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## Demographics of TY 2008 Spanish Free Filers

- 83.7% of TY 2008 Spanish Free Filers earned an AGI of \$25,000 or less.
- 76.7% are age 44 years or younger.
- 77.4% filed as Single or Head of Household.
- 55.7% earned an AGI of \$25,000 or less and are age 44 years or younger and filed as Single or Head of Household.

# *Research Problem 4:*

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**How do the demographic characteristics of Free Filers, Free File Fillable Form users, and Spanish Free Filers compare or differ from each other?**

# Demographic Comparison of Free Filers (FFs), Free File Fillable Form (FFFF) Users, and Spanish Free Filers (SFFs) TY 2008

**Table 21: Top Categories of TY 2008 FF, FFFF, and SFF**

Top Category	FF*	FFFF	SFF
AGI - \$0 to \$17,000	47.7%	40.9%	60.9%
0 Dependents	71.5%	80.4%	52.6%
Simple Return Type	53.1%	60.7%	51.2%
Filing Status - Single	67.1%	69.7%	47.9%
Refund	94.1%	91.9%	93.3%
No EITC	71.0%	90.8%	60.9%
No Education Tax Credit Claimed	93.9%	95.5%	98.5%
No Form 2441 Present	96.6%	97.4%	98.1%
Direct Deposit Accepted	82.2%	82.6%	82.8%
<b>Total Volume</b>	<b>3,009,034</b>	<b>272,600</b>	<b>580</b>

Source: ETA IMF Marketing Database

\*The percent of Free Filers does not include Spanish Free Filers.

- Of the filing attributes that were examined, Table 21 presents the categories with the highest percentage of FF, FFFF, and SFF in TY 2008. The top categories are the same for the three groups.
- These categories were examined independently, so the table does not imply all FF, FFFF, or SFF fall under all of the categories.
- The biggest differences among the three groups occur in 'Zero Dependents' and 'No EITC Claimed'. Also there are significant differences between 'AGI \$0 - \$17,000' and 'Single Filing Status' of the FFFF and SFF groups.
- Over a third (35%) of FF and FFFF are under age 25 years, while SFF has a similar percentage (32%) in the 25 to 34 age group.
- FFFF and SFF with balances due have higher percentage in 'Direct Debit', while FF has higher percentage in 'No Direct Debit'.

# Filing Behavior of TY 2008 Free Filers (FFs), Free File Fillable Form (FFFF) Users, and Spanish Free Filers (SFFs) in TY 2007

**Table 22: Filing Methods of TY 2008 FF, FFFF, and SFF in TY 2007**

TY 2007 Filing Method*	FF	FFFF	SFF
Free File	39.7%	9.7%	9.7%
Online (not FF)	17.0%	12.0%	9.0%
ELF	13.6%	14.8%	30.0%
Paper (not V-Coded)	9.3%	38.5%	3.3%
V-Coded	6.3%	10.4%	20.3%
Not Filed	14.1%	14.6%	27.8%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

\*The percent is based on primary SSNs only.

- TY 2008 FF group has a higher percentage Free Filing than other filing methods in TY 2007, while FFFF group has the highest percentage on true paper filing. Approximately 30% of TY 2008 SFF used Paid-Preparer (ELF) in TY 2007.

**Table 23: TY 2008 1<sup>st</sup> Time Filing Percentage of FF, FFFF, and SFF**

1 <sup>st</sup> Time Filer Indicator	FF	FFFF	SFF
1 <sup>st</sup> Time Filer	6.6%	7.8%	15.5%
Not 1 <sup>st</sup> time Filer	93.4%	92.2%	84.5%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Source: ETA IMF Marketing Database

- Table 23 shows that the percentage of 1<sup>st</sup> time tax return filers using SFF is almost double the percentage using FFFF and more than double the percentage using FF.

# *Research Problem 5:*

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**What can ETARC learn from Free File migration behavior? Specifically, how do eligibility, previous filing behavior and changes in tax situations affect the behavior of First Time Free Filers, Consistent Free Filers, and Drop-out Free Filers?**

# TY 2008 First Time Free Filers

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## Definition

- Taxpayers who used Free File in TY 2008 and did not use Free File in TY 2005, TY 2006, and TY 2007 (but still filed a return each year).
- 957,903 First Time Free Filers

## Questions

- Were First Time Free Filers eligible to Free File based on AGI prior to TY 2008?
- What was the filing behavior of First Time Free Filers prior to TY 2008?
- How did First Time Free Filers' tax situation change or remain the same over the four years?

# Eligibility for Free Filing

**Table 24: Average AGI and Eligibility of TY 2008 First Time Free Filers by Tax Year**

Tax Year	Average AGI	% Eligible
TY 2005	\$24,879	90.1%
TY 2006	\$26,515	90.8%
TY 2007	\$27,043	92.6%
TY 2008	\$24,943	100.0%

Source: ETA IMF Marketing Database

- Most TY 2008 First Time Free Filers were eligible for Free File in prior years.
- 85.3% (817,218) of First Time Free Filers were eligible to Free File based on AGI for all three years prior to TY 2008.

# Preparer Type of TY 2008 First Time Free Filers

**Table 25: Preparer Type of TY 2008 First Time Free Filers by Tax Year**

Preparer Type	TY 2005	TY 2006	TY 2007	TY 2008
Self or VITA	55.9%	56.7%	60.2%	100.0%
Paid	44.1%	43.3%	39.8%	0.0%
Total	100.0% (957,903)	100.0% (957,903)	100.0% (957,903)	100.0% (957,903)

Source: ETA IMF Marketing Database

- Majority of TY 2008 First Time Free Filers self-prepared their returns each year.
- 72.2% (691,708) of First Time Free Filers used the same preparer type for all three years prior to TY 2008.

# Filing Behavior of TY 2008 First Time Free Filers

**Table 26: Filing Method of TY 2008 First Time Free Filers by Tax Year**

Filing Method	TY 2005	TY 2006	TY 2007	TY 2008
ELF	36.5%	37.0%	35.0%	0.0%
Online (Not FF)	20.9%	23.9%	30.4%	0.0%
True Paper	24.9%	23.2%	20.7%	0.0%
V-Coded Paper	17.7%	15.9%	13.8%	0.0%
Free File	0.0%	0.0%	0.0%	100.0%
Total	100.0% (957,903)	100.0% (957,903)	100.0% (957,903)	100.0% (957,903)

Source: ETA IMF Marketing Database

- Majority of TY 2008 First Time Free Filers were already filing electronically in prior years.
- The trend over the years for these First Time Free Filers was a shift towards Online filing.
- 55.6% (532,309) of First Time Free Filers used the same filing method for all three years prior to TY 2008.

# Filing Status of TY 2008 First Time Free Filers

Table 27: Filing Status of TY 2008 First Time Free Filers by Tax Year

Filing Status	TY 2005	TY 2006	TY 2007	TY 2008
Single	49.5%	48.3%	48.1%	48.2%
Married Filing Joint	30.7%	30.9%	30.4%	28.6%
Married Filing Separate	1.9%	2.1%	2.5%	3.8%
Head of Household	17.9%	18.6%	19.0%	19.3%
Widow(er) with Children	0.0%	0.1%	0.1%	0.1%
Married Filing Separate and Spouse not Required to File	0.0%	0.1%	0.0%	0.0%
Total	100.0% (957,903)	100.0% (957,903)	100.0% (957,903)	100.0% (957,903)

Source: ETA IMF Marketing Database

- 74.6% (714,740) of TY 2008 First Time Free Filers used the same filing status all four years.

# TY 2008 First Time Free Filers - Tax Return Complexity and Dependents

**Table 28: Tax Return Complexity of TY 2008 First Time Free Filers by Tax Year**

Return Complexity*	TY 2005	TY 2006	TY 2007	TY 2008
Simple	46.7%	44.3%	43.4%	41.8%
Intermediate	36.3%	35.0%	34.7%	36.0%
Complex	17.0%	20.7%	21.9%	22.2%
<b>Total</b>	<b>100.0%</b> <b>(957,903)</b>	<b>100.0%</b> <b>(957,903)</b>	<b>100.0%</b> <b>(957,903)</b>	<b>100.0%</b> <b>(957,903)</b>

Source: ETA IMF Marketing Database

•See slide 17 for Return Complexity category definitions.

- Although Free File is generally associated with simple returns, First Time Free Filers had a lower proportion of simple returns in the year they switched to Free File.

**Table 29: Dependents of TY 2008 First Time Free Filers by Tax Year**

Dependents	TY 2005	TY 2006	TY 2007	TY 2008
% with No Dependents	61.5%	60.7%	60.6%	61.3%
% with 1 or 2 Dependents	32.2%	32.8%	33.0%	32.6%

Source: ETA IMF Marketing Database

# TY 2008 Consistent Free Filers

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## Definition

- Taxpayers who used Free File in TY 2005, TY 2006, TY 2007, and TY 2008.
- 326,606 Consistent Free Filers

## Questions

- How did Consistent Free Filers' tax situation change or remain the same over the four years?
- Did Consistent Free Filers use the same software company every year?

# Filing Status of Consistent Free Filers

Table 30: Filing Status of Consistent Free Filers by Tax Year

Filing Status	TY 2005	TY 2006	TY 2007	TY 2008
Single	56.7%	55.6%	54.7%	53.7%
Married Filing Joint	23.4%	24.1%	24.9%	25.7%
Married Filing Separate	1.0%	1.0%	1.1%	1.3%
Head of Household	18.9%	19.3%	19.3%	19.2%
Widow(er) with Children	0.0%	0.0%	0.0%	0.0%
Married Filing Separate and Spouse not Required to File	0.0%	0.0%	0.0%	0.0%
Total	100.0% (326,606)	100.0% (326,606)	100.0% (326,606)	100.0% (326,606)

Source: ETA IMF Marketing Database

- 86.3% (281,902) of Consistent Free Filers used the same filing status all four years.

# Consistent Free Filers - Tax Return Complexity and Dependents

**Table 31: Tax Return Complexity of Consistent Free Filers by Tax Year**

Return Complexity*	TY 2005	TY 2006	TY 2007	TY 2008
Simple	50.5%	47.4%	44.1%	42.1%
Intermediate	39.6%	34.4%	35.1%	35.5%
Complex	9.9%	18.3%	20.8%	22.4%
<b>Total</b>	<b>100.0%</b> <b>(326,606)</b>	<b>100.0%</b> <b>(326,606)</b>	<b>100.0%</b> <b>(326,606)</b>	<b>100.0%</b> <b>(326,606)</b>

Source: ETA IMF Marketing Database

• See slide 17 for Return Complexity category definitions.

- The percentage of complex returns increased each year (with the greatest increase from TY 2005 to TY 2006).
- 49.1% (160,193) maintained the same level of return complexity all four years.

**Table 32: Dependents of Consistent Free Filers by Tax Year**

Dependents	TY 2005	TY 2006	TY 2007	TY 2008
% with No Dependents	64.2%	63.2%	62.5%	62.0%
% with 1 or 2 Dependents	30.0%	30.6%	30.8%	31.0%

Source: ETA IMF Marketing Database

- 76.9% (251,206) claimed the same number of dependents all four years.

# Software Use of Consistent Free Filers

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Table 33: Software Use of Consistent Free Filers

Used same Software Every Tax Year	Volume	Percent
Yes	155,980	47.8%
No	170,626	52.2%
Total	326,606	100.0%

Source: ETA IMF Marketing Database

# TY 2005 Drop-Out Free Filers

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## Definition

- Taxpayers who used Free File in TY 2005 and did not use Free File in TY 2006, TY 2007, and TY 2008 (but still filed a return each year).
- 1,763,521 Drop-Out Free Filers

## Questions

- Were Drop-Out Free Filers eligible to Free File based on AGI after TY 2005?
- What was the filing behavior of Drop-Out Free Filers after TY 2005?
- How did Drop-Out Free Filers' tax situation change or remain the same over the four years?

# Eligibility for Free Filing

**Table 34: Average AGI and Eligibility of TY 2005 Drop-Out Free Filers by Tax Year**

Tax Year	Average AGI	% Eligible
TY 2005	\$21,621	100.0%
TY 2006	\$28,780	89.0%
TY 2007	\$34,314	83.2%
TY 2008	\$38,244	79.9 %

Source: ETA IMF Marketing Database

- Most TY 2005 Drop-Out Free Filers were eligible for Free File after TY 2005.
- 75.4% (1,328,734) of Drop-Out Free Filers were eligible to Free File based on AGI for all three years after TY 2005.

# Preparer Type of TY 2005 Drop-Out Free Filers

Table 35: Preparer Type of TY 2005 Drop-Out Free Filers by Tax Year

Preparer Type	TY 2005	TY 2006	TY 2007	TY 2008
Self or VITA	99.9%	76.6%	71.7%	70.7%
Paid	0.1%	23.4%	28.3%	29.3%
Total	100.0% (1,763,521)	100.0% (1,763,521)	100.0% (1,763,521)	100.0% (1,763,521)

Source: ETA IMF Marketing Database

- Majority of TY 2005 Drop-Out Free Filers self-prepared their returns each year.
- 75.4% (1,330,146) of Drop-Out Free Filers used the same preparer type for all three years after TY 2005.

# Filing Behavior of TY 2005 Drop-Out Free Filers

**Table 36: Filing Method of TY 2005 Drop-Out Free Filers by Tax Year**

Filing Method	TY 2005	TY 2006	TY 2007	TY 2008
ELF	0.0%	20.3%	25.0%	26.3%
Online (Not FF)	0.0%	60.1%	57.6%	59.5%
True Paper	0.0%	8.5%	7.5%	6.2%
V-Coded Paper	0.0%	11.1%	9.9%	8.0%
Free File	100.0%	0.0%	0.0%	0.0%
Total	100.0% (1,763,521)	100.0% (1,763,521)	100.0% (1,763,521)	100.0% (1,763,521)

Source: ETA IMF Marketing Database

- Majority of TY 2005 Drop-Out Free Filers continued filing electronically for all three years after TY 2005.
- The migration to Online filing over the years is higher than migration to other filing methods.
- 60.5% (1,067,462) of Drop-Out Free Filers used the same filing method for all three years after TY 2005.

# Filing Status of TY 2005 Drop-Out Free Filers

Table 37: Filing Status of TY 2005 Drop-Out Free Filers by Tax Year

Filing Status	TY 2005	TY 2006	TY 2007	TY 2008
Single	65.9%	58.9%	54.2%	50.6%
Married Filing Joint	20.0%	26.8%	31.4%	34.8%
Married Filing Separate	1.5%	1.4%	1.5%	1.6%
Head of Household	12.6%	12.8%	12.9%	12.9%
Widow(er) with Children	0.0%	0.0%	0.0%	0.0%
Married Filing Separate and Spouse not Required to File	0.0%	0.0%	0.0%	0.0%
Total	100.0% (1,763,521)	100.0% (1,763,521)	100.0% (1,763,521)	100.0% (1,763,521)

Source: ETA IMF Marketing Database

- Drop-Out Free Filers filing as single decreased over the four years, while those married and filed jointly increased.
- 71.5% (1,260,513) of Drop-Out Free Filers used the same filing status all four years.

# TY 2005 Drop-Out Free Filers - Tax Return Complexity and Dependents

**Table 38: Tax Return Complexity of TY 2005 Drop-Out Free Filers by Tax Year**

Return Complexity*	TY 2005	TY 2006	TY 2007	TY 2008
Simple	59.0%	49.8%	44.4%	41.0%
Intermediate	31.5%	31.5%	33.7%	34.9%
Complex	9.5%	18.7%	21.9%	24.1%
<b>Total</b>	<b>100.0%</b> (1,763,521)	<b>100.0%</b> (1,763,521)	<b>100.0%</b> (1,763,521)	<b>100.0%</b> (1,763,521)

Source: ETA IMF Marketing Database

\* See slide 17 for Return Complexity category definitions.

- The percentages filing complex returns increased significantly over the years while the percentage filing simple returns decreased significantly.

**Table 39: Dependents of TY 2005 Drop-Out Free Filers by Tax Year**

Dependents	TY 2005	TY 2006	TY 2007	TY 2008
% with No Dependents	74.8%	71.9%	69.3%	66.9%
% with 1 or 2 Dependents	21.5%	24.0%	26.1%	28.1%

Source: ETA IMF Marketing Database

# Trend Analysis of Some Demographics for the Three Groups across the Four Years

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- **Return Complexity:**

- The percentage of Simple Returns for TY 2008 First Time Free Filers and Consistent Free Filers decreased slightly over the four years, while the percentage of the same return complexity category for TY 2005 Drop-Out Free Filers decreased significantly.
- The percentage of Complex Returns for TY 2008 First Time Free Filers increased moderately over the same period, while the percentage of the same return complexity category for Consistent Free Filers and TY 2005 Drop-Out Free Filers increased significantly.

- **Filing Status:**

- For 'Single' filing status the percentage of TY 2008 First Time Free Filers and Consistent Free Filers decreased moderately over the four years, while the percentage of TY 2005 Drop-Out Free Filers decreased significantly.
- For 'Married Filing Joint' filing status, the percentage of TY 2008 First Time Free Filers decreased slightly over the four years, while the percentage increases for Consistent Free Filers and TY 2005 Drop-Out Free Filers are moderate and significant, respectively.

- **Dependents:**

- The percentage of TY 2008 First Time Free Filers with zero, one, or two dependents remained flat over the four years.
- The percentage of Consistent Free Filers with zero dependents decreased slightly over the same period, while the percentage on TY 2005 Drop-Out Free Filers decreased moderately.
- The percentage increases of Consistent Free Filers and TY 2005 Drop-Out Free Filers with one or two dependents over the same period are slight and moderate, respectively.

# Summary of Findings

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- **Filing Behavior of Free Filers (FFs), Free File Fillable Form (FFFF) Users, and Spanish Free Filers (SFFs)**
  - The majority of TY 2008 FF also used Free Filing in the previous periods TY 2005 – 2007, excluding those taxpayers who did not file in the same period.
  - The majority of TY 2008 FFFF used true paper filing in TY 2007, while the majority of TY 2008 SFF used paid-preparer service for electronic filing in TY 2007.
- **Demographic characteristics of FF, FFFF, and SFF for TY 2008**
  - Most FF, FFFF, and SFF are in the lowest AGI category. SFF has the highest percentage in this AGI category, followed by FF and then FFFF.
  - The majority of FF and FFFF are under age 25 years, while the majority of SFF are in the 25 to 34 age group.
  - A majority of FF, FFFF, and SFF filed as 'Single'. FFFF had the highest percentage filing as 'Single', followed by FF and then SFF.
  - Over 90% of FF, FFFF, and SFF filed with refunds and over 80% of them accepted direct deposit.

# Summary of Findings (continued)

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- **TY 2010 Marketing FF Program**

Within the target group for FF marketing, Self-Prepared Paper Filers with an AGI less than or equal to \$56,000, the highest volume is under 25 years (4.6 M), followed by senior citizens 65 years and over (2.8 M) and the 25 to 34 age group (2.6 M).

- **TY 2010 Marketing FFFF Program**

The highest volume for the target group for FFFF marketing, Self-prepared Paper Filers, is also under 25 years (4.6 M), followed again by senior citizens 65 years and over (3.9 M) and the 25 to 34 age group (3.1 M). These include the volumes of potential taxpayers for the TY 2010 marketing FF program.

- **TY 2010 Marketing SFF Program**

ETARC should focus their marketing of SFF on Spanish-speaking taxpayers 44 years or younger who filed as 'Single' or 'Head of Household' and had an AGI of \$25,000 or less.

# Summary of Findings (Continued)

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- **TY 2008 First Time FF, Consistent FF, and TY 2005 Drop-Out FF**
  - Over 90% of TY 2008 First Time FF and 80% of TY 2005 Drop-Out FF were eligible for Free File in prior years and years after, respectively.
  - A majority of TY 2008 First Time FF and TY 2005 Drop-Out FF filed electronically in prior years and years after, respectively; the percentages of electronic filing over the period increased moderately.
  - A majority of TY 2008 First Time FF and TY 2005 Drop-Out FF self-prepared their returns each year.
  - A majority of the three groups filed as 'Single' each year; the percentage of TY 2008 First Time Free Filers and Consistent Free Filers decreased moderately over the four years while the percentage of TY 2005 Drop-Out Free Filers decreased significantly.
  - A majority of the three groups filed returns with no dependents each year; the percentage of TY 2008 First Time FF remained flat over the four years; the percentage of Consistent FF decreased slightly over the same period, while the percentage of TY 2005 Drop-Out FF decreased moderately.
  - A majority of the three groups used 'Simple' returns each year. The percentage of Simple Returns for TY 2008 First Time Free Filers and Consistent Free Filers decreased slightly over the four years, while the percentage of the same return complexity category for TY 2005 Drop-Out Free Filers decreased significantly.

# Approval Statement

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**This report has been approved by the Director,  
Wage & Investment Research and Analysis.**