



441 G St. N.W.
Washington, DC 20548

Accessible Version

April 9, 2024

The Honorable Danny Werfel
Commissioner
Internal Revenue Service

IRS Direct File: Actions Needed during Pilot to Improve Information on Costs and Benefits

Dear Mr. Werfel:

In connection with our ongoing audit of the Internal Revenue Service’s (IRS) Direct File pilot, we found IRS has not produced comprehensive cost and benefit estimates needed to inform decision-making postpilot. Collecting relevant data during the pilot would allow IRS to improve its estimates.

Direct File is intended to provide taxpayers with a new free option for preparing and filing a tax return on irs.gov. Once mature, a government-run tax filing system could save taxpayers time and money, make it easier to claim tax benefits, and provide several benefits to IRS. IRS has been working with the U.S. Digital Service, taxpayers, state revenue offices and others, to design, build, and pilot a user-friendly system. Members of Congress and other observers have raised questions about how much funding will be required to support such a system, including the long-term provision of a sufficient level of customer service.

The Inflation Reduction Act of 2022 (IRA) includes a provision for GAO to oversee the distribution and use of IRA funds, including funds related to Direct File.¹ This report focuses on IRS’s estimates of the costs and benefits of Direct File and opportunities to use the pilot to collect data to improve those estimates to inform future decisions. IRS’s early efforts related to the pilot have been focused on how to improve the taxpayer experience through Direct File. We expect to report on those efforts later this year as part of a more extensive, ongoing evaluation of the pilot.

For this report, we compared IRS’s initial cost estimates for Direct File in the agency’s May 2023 report to Congress against best practices for cost estimation and economic analysis as well as IRS’s goal of ensuring a cost-effective Direct File system.² We compared IRS’s initial benefit estimates against relevant requirements for improving the customer experience when using

¹Pub. L. No. 117-169, tit. VII, § 70004, 136. Stat. 1818, 2087 (2022).

²GAO, *Cost Estimating and Assessment Guide: Best Practices for Developing and Managing Program Costs*, [GAO-20-195G](#) (Washington, D.C.: Mar. 12, 2020), *Assessment Methodology for Economic Analysis*, [GAO-18-151SP](#) (Washington, D.C.: Apr. 10, 2018); and Internal Revenue Service, *Internal Revenue Service Inflation Reduction Act Strategic Operating Plan: FY2023–2031* (Washington, D.C.: Apr. 5, 2023).

federal services and best practices for economic analysis.³ We also reviewed IRS plans for evaluating the results of the Direct File pilot.⁴ We interviewed IRS officials and reviewed a relevant report by the Treasury Inspector General for Tax Administration.

We conducted this performance audit from December 2023 to April 2024 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Background

The IRA provided IRS tens of billions of dollars to improve taxpayer service and achieve other objectives, such as expanding enforcement.⁵ It also directed IRS to report on the cost of developing and running a system that would allow taxpayers to prepare and file their tax returns for free on irs.gov.⁶ In May 2023, IRS reported to Congress that the annual costs could range from \$64 million to \$249 million depending on the number of taxpayers served and the complexity of tax situations supported by Direct File. IRS noted several uncertainties in the estimates, such as the number of taxpayers who may choose to use the Direct File system.⁷

On the same day that IRS submitted its report to Congress, the Deputy Secretary of the Treasury directed IRS to pilot a Direct File system during the 2024 tax filing season. The pilot launched in January 2024 and allows certain taxpayers to prepare and file their tax returns for free on irs.gov using a question-and-answer format. IRS has budgeted \$114 million for Direct File in fiscal year 2024 with funding coming from three appropriations accounts:

- \$50 million for business systems modernization,
- \$38 million for taxpayer services, and
- \$26 million for operations support.

As of January 31, 2024, IRS officials reported that approximately \$9.4 million of these funds have been obligated for Direct File activities. The pilot is currently available to taxpayers with simple tax situations who reside in one of 12 states: Arizona, California, Florida, Massachusetts, New Hampshire, New York, Nevada, South Dakota, Tennessee, Texas, Washington, and

³Exec. Order No. 14058, *Transforming Federal Customer Experience and Service Delivery To Rebuild Trust in Government*, 86 Fed. Reg. 71357 (Dec. 13, 2021); and [GAO-18-151SP](#).

⁴We reviewed the following documents provided in January 2024: *IRS Direct File: Pilot Evaluation Review* (Jan. 11, 2024); *Direct File 2024 Pilot Gating Criteria Plan v0.2*; and *Draft DF Metrics (00B)*. IRS officials noted that information in these documents may continue to evolve. We will refer to these documents as IRS's pilot evaluation plans.

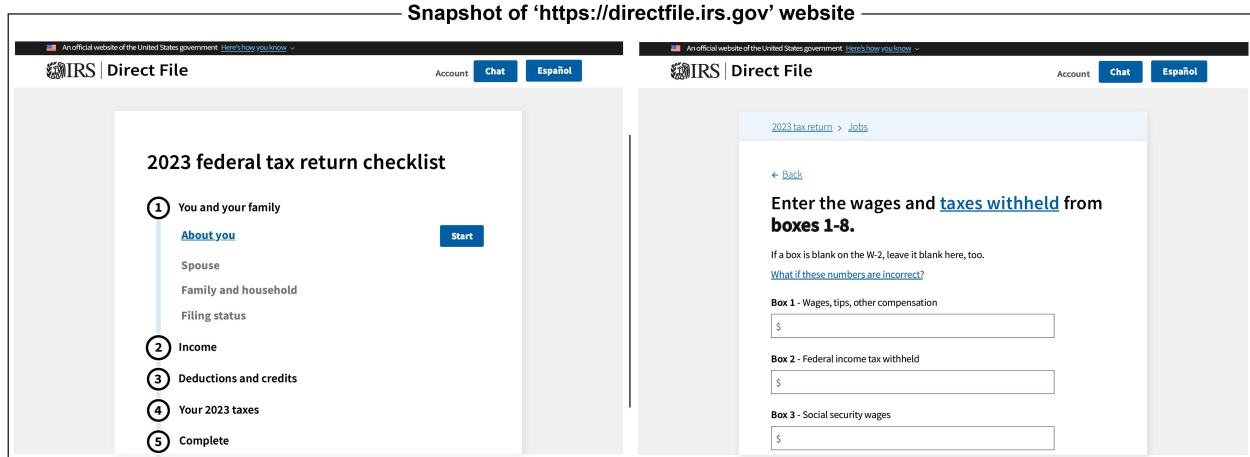
⁵The IRA appropriated \$79.4 billion for IRS. Pub. L. No. 117-169, § 10301, 136 Stat. at 1831–1832. In June 2023, the Fiscal Responsibility Act of 2023 rescinded about \$1.4 billion of amounts appropriated for IRS by the IRA. Pub. L. No. 118-5, div. B, tit. II, § 251, 137 Stat. 10, 30-31 (2023).

⁶Pub. L. No. 117-169, § 10301(1)(B), 136 Stat. at 1832. IRS refers to the system being piloted as Direct File and this report will use that term. Such a system is sometimes referred to as a direct e-file.

⁷Department of the Treasury, Internal Revenue Service, *IRS Report to Congress: Inflation Reduction Act §10301(1)(B) IRS-run Direct e-File Tax Return System*, Publication 5788 (Washington, D.C.: May 16, 2023).

Wyoming. Participating taxpayers answer interview style questions on an IRS website (<https://directfile.irs.gov>) to complete and file an electronic tax return for free (see fig. 1).

Figure 1: IRS Direct File Interface as of January 2024



Source: IRS. | GAO-24-107236

The scope of the pilot includes wage income, Social Security income, unemployment benefits, and interest income of \$1,500 or less. Participants must claim the standard deduction. Taxpayers participating in the pilot may also claim the Earned Income Tax Credit, the Child Tax Credit, and the Credit for Other Dependents, and they may deduct student loan interest and educator expenses. Other credits and deductions are not available through the pilot for the 2024 tax filing season. Officials plan to conclude the pilot in late April 2024 shortly after the end of the tax filing season.

Direct File Cost Estimates Provided to Congress Were Not Comprehensive

Direct File cost estimates that IRS provided in its May 2023 report to Congress did not fully align with best practices for cost estimation. IRS's report stated its estimates included the cost of developing and maintaining a secure, multilingual, mobile-friendly tax filing tool and its underlying technology to keep pace with changes to tax law, as well as the cost of providing customer support. Along with its cost estimates, IRS described underlying assumptions, a recommended practice to help inform decision-makers of the estimate's scope.⁸ IRS's cost estimates assumed that a Direct File system would start with a limited tax scope and that moderate, steady spending over time would be needed to keep the technology up to date as tax law changes.

IRS's estimates also included elements of a sensitivity analysis, another recommended practice, to demonstrate how changes in underlying assumptions may affect the estimates.⁹ Specifically, IRS described how costs were expected to change depending on the number of taxpayers served and the complexity of the tax situations supported.

⁸GAO-20-195G.

⁹GAO-20-195G.

However, IRS's cost estimates did not address other recommended practices, such as ensuring all costs were included and documented. A review by the Treasury Inspector General for Tax Administration found that IRS had no documentation to support the underlying data, analysis, or assumptions used for Direct File cost estimates.¹⁰ We found this as well. A best practice for economic analysis is a transparent methodology, including analytical choices and assumptions.¹¹

IRS officials also told us that Direct File cost estimates did not include start-up costs, such as technology for a novel system, which could be substantial. A best practice for cost estimation is to include development costs as part of a complete cost estimate.¹² Without a comprehensive accounting for costs, estimates could understate the full amount of resources required for IRS to develop and maintain a permanent Direct File program.

Our recent work on IRS agency reform identified weaknesses in IRS's policies and procedures for developing cost estimates.¹³ We found that IRS does not have a comprehensive policy for non-IT cost estimation. We also found IRS procedures for estimating IT costs address, but do not fully meet, all cost estimation best practices. In response to our recommendations, IRS plans to document its policies in this area and use best practices for cost estimation as appropriate. By taking action to address our prior recommendations, IRS would have policies in place for evaluating projects and initiatives in its strategic operating plan for using IRA funds.

IRS Risks Missing Opportunities to Use the Pilot to Improve Cost and Benefit Estimates for Direct File

Costs

The Direct File pilot provides opportunities for IRS to improve its cost estimates. IRS officials stated that they will update the cost estimates for the program after the pilot. However, we found insufficient documentation to provide reasonable assurance that the pilot will capture the necessary data to inform more complete cost estimates. According to documentation and IRS officials, the current focus is to evaluate critical operational aspects of the pilot. However, IRS officials risk missing time-sensitive opportunities to inform cost estimates in several categories:

- **Customer service costs.** The Direct File pilot presents several opportunities to improve estimates of customer service costs for a permanent program. For example, IRS is training 400 customer service representatives on Direct File and the cost of their training could be estimated. Also, as the customer service representatives begin to assist taxpayers using the new Direct File system, IRS will have the opportunity to measure the time spent on Direct File assistance and use that information to help determine the cost of customer service for a Direct File program. IRS officials told us they will have the necessary data to estimate customer service costs following the pilot. For example, the data will include time spent on Direct File that customer service representatives record on their timecards. In discussions

¹⁰Treasury Inspector General for Tax Administration, *Inflation Reduction Act: Assessment of a Free and Electronic Direct Filing Tax Return System*, 2024-408-002 (Washington, D.C.: Oct. 2, 2023).

¹¹[GAO-18-151SP](#).

¹²[GAO-20-195G](#).

¹³GAO, *IRS Reform: Following Leading Practices and Improving Cost Estimation Policies Could Benefit Agency Efforts*, [GAO-24-106091](#) (Washington, D.C.: Feb. 14, 2024).

with officials, they noted that timecard data would allow a retrospective calculation of how much Direct File assistance cost during the 2024 pilot. However, IRS has not yet identified a methodology for using timecard data to project costs for potential future expansions of the pilot.

IRS's pilot evaluation plans identified several potential metrics related to Direct File customer service, such as counting taxpayer interactions with customer service representatives, measuring the time required to resolve issues, and categorizing the type of issues for which taxpayers are seeking assistance. However, IRS identified no metrics for estimating potential future customer service costs.

When the agency outlined its strategic operating plan for using IRA funding in April 2023, it sought to study the extent to which a Direct File system is "feasible, cost-effective, secure, and meets the needs of taxpayers." In the report to Congress, IRS estimated that the majority of Direct File costs could result from customer service expenses. Unless IRS collects sufficient customer service data to inform its customer service cost estimates, it will be difficult for decision-makers to determine the feasibility of a permanent or expanded Direct File system.

- **Technology costs.** IRS's report to Congress noted that a Direct File system would require "frequent updates" to reflect tax law changes. On January 31, 2024, the House of Representatives passed a bill that would make changes to the Child Tax Credit, which can be claimed using the Direct File system.¹⁴ As of April 2, 2024, the Senate continues to consider the legislation. In addition to potential tax law changes, IRS may need to update Direct File technology in response to taxpayer feedback. IRS's pilot evaluation plans, which were finalized prior to the introduction of this legislation, do not address such changes. However, officials told us they plan to track the time required to update the Direct File system if changes are made to the Child Tax Credit.
- **Cost of integrating state returns.** IRS research determined that many taxpayers prefer to use the same system to prepare and file federal, state, and local income tax returns so that information can be carried over from the federal to state return.¹⁵ IRS seeks to use the Direct File pilot to gain experience in this area, which provides an opportunity to collect information on the cost of transferring data from IRS's Direct File system to similar state-level systems. Five of the 43 states with income taxes are participating in the Direct File pilot.¹⁶ Collecting information during the pilot on the cost of integrating state tax returns could help inform decisions on including taxpayers from the remaining 38 states in Direct File.

IRS officials noted that they are piloting a process to transfer data to three of the participating states' returns: Arizona, Massachusetts, and New York.¹⁷ If these efforts prove successful, officials believe taxpayers from more states could be supported without significant additional costs for the federal government. However, officials were unsure how

¹⁴H.R. 7024, 118th Cong. (2024). The bill also includes provisions related to depreciation allowances, the low-income housing credit, and losses due to natural disasters, among other provisions.

¹⁵IRS cited a survey conducted by the MITRE Corporation.

¹⁶Arizona, California, Massachusetts, and New York tax income and are participating in the pilot. Washington State taxes the sale or exchange of long-term capital assets and, for purposes of the pilot, IRS will direct Washington taxpayers to the appropriate state filing tool to claim a state-level working families tax credit.

¹⁷IRS officials described developing a technical process called an application program interface or API.

they could estimate these potential costs during the 2024 pilot. While officials said they would include the cost of developing the data transfer process in estimating the cost of the pilot, the pilot evaluation plans focus more on operational issues, such as how to make the experience of state tax filing more seamless for taxpayers. The evaluation plan contains no metrics estimating costs related to state tax return integration and does not identify potential challenges which could present unexpected future expenses for IRS or state tax administrators.

Taxpayers in two states will not have their federal data transferred to their state revenue agencies. Memorandum of understanding between IRS and revenue agencies in California and Washington reflect the states' request for limited participation in the pilot with no integration with IRS's Direct File system. For these states, IRS directs taxpayers to state-administered tax filing systems upon completion of the federal return.

- **Cost of supporting additional tax situations.** IRS's pilot evaluation plans do not describe how the agency can use data collection opportunities provided by the pilot to estimate the incremental cost of gradually expanding the Direct File system's capabilities. Even the limited scope of the 2024 tax filing season pilot required substantial work by IRS officials to develop the question-and-answer prompts used to collect relevant information from taxpayers to populate their tax returns on irs.gov. Specifically, officials tested draft questions with taxpayers to obtain live feedback and all material had to go through legal review. This activity provides an opportunity to estimate the potential costs of adding new capabilities.
- **Additional labor costs.** IRS's spending estimates described above do not account for the full cost of Direct File for fiscal year 2024. To build and run the pilot, IRS is using 29 employees from the U.S. Digital Service (USDS) to supplement IRS employees.¹⁸ Officials said USDS developed the prototype that evolved into the Direct File system. IRS is not required to reimburse USDS for its employees, and officials reported no cost to IRS for the prototype.¹⁹ A complete cost estimate should cover all costs anticipated during the lifespan of a Direct File system and cover multiple fiscal years.²⁰ IRS officials could not provide information on the USDS resources used for Direct File.

A full accounting of all labor, material, and other efforts required to develop and run a Direct File system can help inform postpilot decision-making.²¹ Complete cost information informs decisions about whether the pilot should be made permanent and decisions about program design tradeoffs such as what additional tax situations to support.

¹⁸The U.S. Digital Service is part of the Executive Office of the President's Office of Management and Budget. The number of employees is from January 2024.

¹⁹Officials said the prototype was developed for taxpayer user research to inform the report to Congress. IRS is also receiving support from the General Services Administration's Office of 18F within the Technology Transformation Services' Office of Client and Markets, which is reimbursed by IRS for its services.

²⁰[GAO-20-195G](#).

²¹[GAO-20-195G](#).

Benefits

In addition to considering potential costs, it is also important to consider the potential benefits to taxpayers and IRS of a free, government-run, online tax filing system. The pilot provides opportunities to inform related IRS research.

IRS estimates that the Direct File pilot for the 2024 tax filing season will save taxpayers \$21 million using the assumption that approximately 500,000 taxpayers participate.²² The estimate assumes that taxpayers avoid paying commercial preparers or a tax professional for assistance in preparing a return. The concept of taxpayer compliance burden refers to the costs of such commercial services and also includes the time taxpayers spend preparing and filing a return.²³

Officials told us that they expect little change in the time Direct File users spend completing a tax return compared to using commercial software. IRS plans to survey a stratified random sample of 5,000 Direct File participants in fiscal years 2024 and 2025 to estimate the burden incurred by all Direct File users as well as compare their burden to similarly situated taxpayers who used other tax return preparation methods, according to officials. IRS is working to finalize questions and a survey plan by mid-March 2024 and the fiscal year 2024 survey will be conducted between April 2024 and May 2025.²⁴ Officials also stated that they plan to interview taxpayers.

In addition to potential reductions in the compliance burden for taxpayers, IRS identified other potential benefits of Direct File, such as making it easier for eligible taxpayers to claim credits and deductions, reducing the volume of paper returns, and reducing errors. IRS's pilot evaluation plans state that research officials will analyze the extent to which taxpayers take credits and deductions they may be eligible for but did not previously take. However, IRS's pilot evaluation plans do not identify metrics to evaluate the extent to which additional taxpayers claim benefits to which they are entitled. The interviews described above for analyzing the compliance burden could also be an opportunity to ask taxpayers if the Direct File system made it easier to obtain certain tax benefits.

IRS's pilot evaluation plans have also not identified metrics for evaluating potential benefits related to reducing paper returns and errors. IRS research officials estimated in August 2023 that there are approximately 200,000 paper filers who may be eligible to participate in the Direct File pilot. IRS's pilot evaluation plans from January 2024 state that it intends to analyze how many taxpayers switch to the pilot from paper filing. IRS officials believe that some paper filers may have used that method in the past to avoid paying for commercial services.

IRS officials also plan to compare the extent to which taxpayers using Direct File need to submit amended returns compared to existing filing options. These additional opportunities to collect data during the pilot could help IRS quantify potential reductions in administrative costs. Officials agreed that they would need to assess data in this area following the pilot.

²²This estimate is contained in a supporting statement IRS provided to the Office of Management and Budget seeking that office's permission to collect information from taxpayers for the individual income tax return.

²³An IRS survey on this topic refers to the concept as taxpayer burden. The compliance burden does not include the money a taxpayer may pay in taxes. See GAO, *Understanding the Tax Reform Debate: Background, Criteria, & Questions*, [GAO-05-1009SP](#) (Washington, D.C.: Sept. 1, 2005).

²⁴Officials said the survey will pertain to tax year 2023 returns.

An executive order directs the Secretary of the Treasury to design and deliver new online services and tools to ease the payment of taxes and states that the government's performance in improving the customer experience must be measured empirically.²⁵ Further, a best practice for economic analysis is to quantify potential benefits and monetize benefits when feasible to inform decision-makers more fully.²⁶ IRS risks missing important opportunities during its Direct File pilot to collect the data necessary to assess the extent to which a Direct File system could improve the taxpayer experience.

Officials told us in February 2024 that senior leadership had not decided on the future of the pilot beyond the 2024 tax filing season. Officials told us that the time required to continue Direct File would depend on several factors: whether issues identified in the 2024 pilot would need to be addressed, whether any new capabilities are to be added, and the size of the team working on Direct File. Officials noted that hiring new employees is a lengthy process. USDS employees helping IRS during the pilot are scheduled to complete their assignments in September 2024. IRS officials reported in March 2024 that they are considering whether USDS could provide support for additional time.

While IRS officials believe that cost estimates can be improved following the 2024 tax filing season and the pilot, officials will have a short amount of time to analyze cost and benefit information before making decisions about the future of Direct File for the 2025 tax filing season. IRS's strategic operating plan for using IRA funds states that it seeks to ensure a Direct File system is feasible, cost effective, and secure, and meets the needs of taxpayers before the agency offers a new online service. Without collecting the information needed during the 2024 pilot to inform a comprehensive assessment of the costs associated with Direct File and its benefits, IRS risks making longer-term decisions without full information. Taken together, these steps should help support data-driven evaluation by IRS leadership and members of Congress.

Recommendations for Executive Action

We are making the following three recommendations to IRS:

The Commissioner of Internal Revenue should ensure that relevant officials apply best practices to estimate and document the full costs of developing and operating a Direct File system. (Recommendation 1)

The Commissioner of Internal Revenue should ensure that relevant officials estimate and document the potential benefits of a Direct File system. (Recommendation 2)

The Commissioner of Internal Revenue should use the cost and benefit data collected during the pilot along with other relevant considerations to inform future decisions about the Direct File system. (Recommendation 3)

Agency Comments

We provided a draft of this report to IRS for review and comment. IRS agreed with all of our recommendations. In its comments, reproduced in enclosure I, IRS described planned actions consistent with all our recommendations. In summary, IRS stated that information gathered

²⁵Exec. Order No. 14058, *Transforming Federal Customer Experience and Service Delivery To Rebuild Trust in Government*, 86 Fed. Reg. 71359 (Dec. 13, 2021).

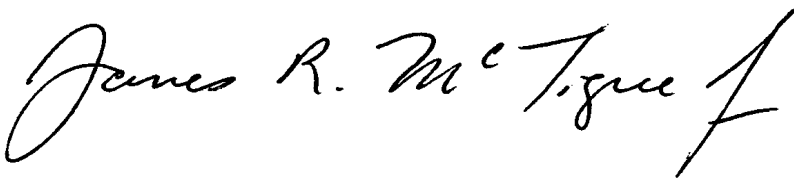
²⁶[GAO-18-151SP](#).

during the pilot will help it develop an accurate baseline for estimating the costs and benefits of a Direct File system. IRS stated that cost and benefit data will help inform a decision on the future of Direct File. IRS also provided technical comments, which we incorporated as appropriate.

We are sending copies of this report to the appropriate congressional committees. In addition, the report is available at no charge on the GAO website at <https://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at 202-512-6806 or McTigueJ@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Staff who made key contributions to this report were, Tara Carter, Assistant Director; Michael O'Neill, Analyst in Charge; Adrian Arcoleo, Rob Gebhart, Abigail Loxton, Dan Mahoney, Jesse Mitchell, Robert Robinson, and Andrew J. Stephens.

Sincerely,

A handwritten signature in black ink that reads "James R. McTigue, Jr." with a stylized flourish at the end.

James R. McTigue, Jr.
Director, Tax Policy and Administration
Strategic Issues
Enclosure I

Enclosure I: Comments from the Internal Revenue Service



COMMISSIONER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

March 29, 2024

Mr. James R. McTigue, Jr.
Director, Tax Policy and Administration
U.S. Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

Dear Mr. McTigue:

I have reviewed Government Accountability Office's (GAO's) DRAFT Interim Report titled: "*IRS Direct File: Actions Needed During Pilot to Improve Information on Costs and Benefits*," and welcome the opportunity to provide a response. I appreciate that GAO recognizes that Direct File has the potential to save taxpayers time and money while also making it easier for taxpayers to claim tax benefits. The IRS will learn a lot from the current pilot that will help inform the future of Direct File.

We are aware that the IRS's cost estimates contained in the Direct File report to Congress may not have contained the level of detail or supporting documentation that GAO and others have requested, which is in part due to the lack of baseline or comparable data available. This year's Direct File pilot will serve as that baseline should the IRS and the Department of the Treasury decide to move forward with Direct File in future years. We agree with GAO that the pilot provides opportunities for the IRS to improve its cost estimates. Information gathered throughout the duration of the pilot will allow us to develop an accurate baseline for this novel government service.

Direct File is a completely new service offered by the IRS and, in terms of technology and customer support, is not something the IRS or other federal agencies have offered before. Unlike other government technology projects like student loan relief, passport applications, and the Free Application for Federal Student Aid (FAFSA), Direct File is not the only option for taxpayers but is one of many options available for taxpayers to fulfill their tax filing obligations.

We agree with GAO that a full accounting of all costs required to develop and deliver the Direct File pilot will be helpful in producing updated cost estimates for Direct File that will help inform post-pilot decision-making, and we are working on those

estimates now.¹ Until a baseline for estimating those costs can be developed, we have relied on metrics on different aspects of the pilot. These metrics, together with the actual costs incurred in the development and delivery of the pilot, will help inform the updated cost estimates that we are developing.

Customer service costs

We are tracking several metrics related to customer support throughout the pilot, including the number of chats, wait time, average handle time, and shifting demand throughout the day and the filing season as a whole. Measuring the time spent by Customer Service Representatives (CSRs) on providing live chat assistance to Direct File users, combined with the number of chats coming into Direct File and the number of assistants staffing the chat, will allow the IRS to determine how many assistants are needed for Direct File customer support. This will in turn lead to more accurate projections for the cost of customer support.

Technology costs

Direct File was built in a way to ensure it was configurable and could be updated to reflect the ever-changing Internal Revenue Code. Should any tax law changes pass during the pilot, the IRS will track how long it takes to implement those changes to better estimate additional costs for the future.

Costs of integrating state returns

One of the challenges in developing the pilot was in the ability to create a seamless experience for taxpayers to file both their federal and state taxes. We know from our Report to Congress this is an issue that drives interest in Direct File, and we wanted to understand our ability to deliver a simple and secure experience. One of the things we are looking to learn through the pilot is the success of the Direct File data transfer Application Programming Interface (API), and, if successful, how much effort would be involved in extending this option to additional states. This information will help inform our updated cost estimates.

Costs of supporting additional tax situations

As GAO notes, the limited scope of the pilot required substantial work to develop the tax logic and flow to support the tax scope, the drafting and reviewing of hundreds of pages of content, and user testing with taxpayers to ensure the content is both easy to understand and accurate. Based on our experience developing the pilot, the IRS is better positioned to produce estimates that include the cost of supporting additional tax situations in the future.

Additional labor costs

The IRS has been fortunate in the development of the Direct File pilot to work in partnership with technology experts at the United States. Digital Service (USDS) and the Government Services Administration's 18F organization. While their support of

¹ While GAO notes that a best practice for cost estimates is to include start-up costs, after the conclusion of the Direct File pilot, we will be able to provide actual startup costs for the delivery of the pilot.

Direct File may not continue long term, any cost estimate for potential future years of Direct File will include staffing costs. *Benefits*

Direct File cost estimates should also be considered in conjunction with an analysis of the potential benefits that Direct File provides to both taxpayers and the IRS, in terms of both time and money, and that work will continue after the pilot. As noted, Direct File will be part of the IRS's annual Individual Taxpayer Burden (ITB) survey to help understand its impact on the burden associated with taxpayers filing a tax return. Additionally, the IRS plans extensive post-pilot analysis of several issues, including:

- Tax returns filed through Direct File by taxpayers who previously filed on paper;
- Potential increase in taxpayers who claimed credits and benefits they were entitled to but previously did not claim; and
- The need for amended returns for taxpayers filing through Direct File compared with other filing methods.

While these analyses will be longer term and not available immediately after the pilot concludes, they will be critical to helping the IRS understand the potential benefits associated with moving forward with Direct File in the future.

The IRS takes seriously its need to fully evaluate the Direct File pilot to understand its impacts. The data gathered and lessons learned throughout the pilot will help inform a decision on the future of Direct File. This includes providing actual costs of the pilot, along with an analysis of its benefits. We are collecting extensive data throughout the pilot that will help inform that analysis.

The IRS always appreciates GAO's role in helping improve the Federal Government.

Our responses to your specific recommendations are enclosed. If you have any questions, please contact me, or a member of your staff may contact the Direct File, Chief, Bridget Roberts, at 202-317-4212.

Sincerely

Daniel I.
Werfel
Danny I. Werfel
Commissioner
Internal Revenue Service

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I. Werfel
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Enclosure

Enclosure

GAO Recommendations and IRS Responses to GAO Draft Report
IRS Direct File: Actions Needed During Pilot to Improve Information on Costs and Benefits (GAO-24-107236)

RECOMMENDATION 1

The Commissioner of Internal Revenue should ensure that relevant officials apply best practices to estimate and document the full costs of developing and operating a Direct File system.

COMMENT

The IRS agrees with this recommendation and will apply best practices to estimate and document the full costs of developing and operating Direct File. As noted in our response to the draft report entitled *IRS Reform: Following Leading Practices and Improving Cost Estimation Policies Could Benefit Agency Efforts* (GAO-24-106091), the IRS has a mature cost estimation process for its labor and information technology (IT) programs that follows most of the twelve best practices identified in GAO's cost estimation guide. The IRS is in the process of formalizing its existing non-IT and IT estimation guidance used by practitioners across the Service by including it as policy in the Internal Revenue Manual and is also finalizing interim guidance that will be released later this year. This guidance will help ensure that the IRS applies best practices to estimate and document the costs of developing and operating the Direct File system moving forward.

RECOMMENDATION 2

The Commissioner of Internal Revenue should ensure that relevant officials estimate and document the potential benefits of a Direct File system.

COMMENT

The IRS agrees with this recommendation and plans to evaluate the benefits of the Direct File system, including analyzing the taxpayer burden of Direct File users compared to taxpayers who used other tax return preparation methods, analyzing the extent to which taxpayers take credits and deductions, and identifying the extent to which paper filings may have been reduced. The IRS plans to document and quantify these benefits to ensure decisions made about the future of Direct File are data-driven and based on a comprehensive analysis of both costs and benefits along with other relevant considerations.

RECOMMENDATION 3

The Commissioner of Internal Revenue should use the cost and benefit data collected during the pilot along with other relevant considerations to inform future decisions about the Direct File system.

COMMENT

The IRS agrees with this recommendation. The Commissioner will use the cost and benefit data collected during the pilot along with other relevant considerations to inform future decisions about Direct File.

Accessible text for Enclosure I: Comments from the Internal Revenue Service

March 29, 2024

Mr. James R. McTigue, Jr.
Director, Tax Policy and Administration
U.S. Government Accountability Office 441 G Street, N.W.
Washington, DC 20548

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We are aware that the IRS's cost estimates contained in the Direct File report to Congress may not have contained the level of detail or supporting documentation that GAO and others have requested, which is in part due to the lack of baseline or comparable data available. This year's Direct File pilot will serve as that baseline should the IRS and the Department of the Treasury decide to move forward with Direct File in future years. We agree with GAO that the pilot provides opportunities for the IRS to improve its cost estimates. Information gathered throughout the duration of the pilot will allow us to develop an accurate baseline for this novel government service.

Direct File is a completely new service offered by the IRS and, in terms of technology and customer support, is not something the IRS or other federal agencies have offered before. Unlike other government technology projects like student loan relief, passport applications, and the Free Application for Federal Student Aid (FAFSA), Direct File is not the only option for taxpayers but is one of many options available for taxpayers to fulfill their tax filing obligations.

We agree with GAO that a full accounting of all costs required to develop and deliver the Direct File pilot will be helpful in producing updated cost estimates for Direct File that will help inform post-pilot decision-making, and we are working on those estimates now.¹ Until a baseline for estimating those costs can be developed, we have relied on metrics on different aspects of the pilot. These metrics, together with the actual costs incurred in the development and delivery of the pilot, will help inform the updated cost estimates that we are developing.

Customer service costs

We are tracking several metrics related to customer support throughout the pilot, including the number of chats, wait time, average handle time, and shifting demand throughout the day and the filing season as a whole. Measuring the time spent by Customer Service Representatives (CSRs) on providing live chat assistance to Direct File users, combined with the number of chats coming into Direct File and the number of assistants staffing the chat, will allow the IRS to

¹ While GAO notes that a best practice for cost estimates is to include start-up costs, after the conclusion of the Direct File pilot, we will be able to provide actual startup costs for the delivery of the pilot.

determine how many assistors are needed for Direct File customer support. This will in turn lead to more accurate projections for the cost of customer support.

Technology costs

Direct File was built in a way to ensure it was configurable and could be updated to reflect the ever-changing Internal Revenue Code. Should any tax law changes pass during the pilot, the IRS will track how long it takes to implement those changes to better estimate additional costs for the future.

Costs of integrating state returns

One of the challenges in developing the pilot was in the ability to create a seamless experience for taxpayers to file both their federal and state taxes. We know from our Report to Congress this is an issue that drives interest in Direct File, and we wanted to understand our ability to deliver a simple and secure experience. One of the things we are looking to learn through the pilot is the success of the Direct File data transfer Application Programming Interface (API), and, if successful, how much effort would be involved in extending this option to additional states. This information will help inform our updated cost estimates.

Costs of supporting additional tax situations

As GAO notes, the limited scope of the pilot required substantial work to develop the tax logic and flow to support the tax scope, the drafting and reviewing of hundreds of pages of content, and user testing with taxpayers to ensure the content is both easy to understand and accurate. Based on our experience developing the pilot, the IRS is better positioned to produce estimates that include the cost of supporting additional tax situations in the future.

Additional labor costs

The IRS has been fortunate in the development of the Direct File pilot to work in partnership with technology experts at the United States Digital Service (USDS) and the Government Services Administration's 18F organization. While their support of Direct File may not continue long term, any cost estimate for potential future years of Direct File will include staffing costs.

Benefits

Direct File cost estimates should also be considered in conjunction with an analysis of the potential benefits that Direct File provides to both taxpayers and the IRS, in terms of both time and money, and that work will continue after the pilot. As noted, Direct File will be part of the IRS's annual Individual Taxpayer Burden (ITB) survey to help understand its impact on the burden associated with taxpayers filing a tax return. Additionally, the IRS plans extensive post-pilot analysis of several issues, including:

- Tax returns filed through Direct File by taxpayers who previously filed on paper;
- Potential increase in taxpayers who claimed credits and benefits they were entitled to but previously did not claim; and
- The need for amended returns for taxpayers filing through Direct File compared with other filing methods.

While these analyses will be longer term and not available immediately after the pilot concludes, they will be critical to helping the IRS understand the potential benefits associated with moving forward with Direct File in the future.

The IRS takes seriously its need to fully evaluate the Direct File pilot to understand its impacts. The data gathered and lessons learned throughout the pilot will help inform a decision on the future of Direct File. This includes providing actual costs of the pilot, along with an analysis of its benefits. We are collecting extensive data throughout the pilot that will help inform that analysis.

The IRS always appreciates GAO's role in helping improve the Federal Government.

Our responses to your specific recommendations are enclosed. If you have any questions, please contact me, or a member of your staff may contact the Direct File, Chief, Bridget Roberts, at 202-317-4212.

Sincerely,

Danny I. Werfel
Commissioner
Internal Revenue Service

Enclosure

GAO Recommendations and IRS Responses to GAO Draft Report

IRS Direct File: Actions Needed During Pilot to Improve Information on Costs and Benefits (GAO-24-107236)

RECOMMENDATION 1

The Commissioner of Internal Revenue should ensure that relevant officials apply best practices to estimate and document the full costs of developing and operating a Direct File system.

COMMENT

The IRS agrees with this recommendation and will apply best practices to estimate and document the full costs of developing and operating Direct File. As noted in our response to the draft report entitled IRS Reform: Following Leading Practices and Improving Cost Estimation Policies Could Benefit Agency Efforts (GAO-24-106091), the IRS has a mature cost estimation process for its labor and information technology (IT) programs that follows most of the twelve best practices identified in GAO's cost estimation guide. The IRS is in the process of formalizing its existing non-IT and IT estimation guidance used by practitioners across the Service by including it as policy in the Internal Revenue Manual and is also finalizing interim guidance that will be released later this year. This guidance will help ensure that the IRS applies best practices to estimate and document the costs of developing and operating the Direct File system moving forward.

RECOMMENDATION 2

The Commissioner of Internal Revenue should ensure that relevant officials estimate and document the potential benefits of a Direct File system.

COMMENT

The IRS agrees with this recommendation and plans to evaluate the benefits of the Direct File system, including analyzing the taxpayer burden of Direct File users compared to taxpayers who used other tax return preparation methods, analyzing the extent to which taxpayers take credits and deductions, and identifying the extent to which paper filings may have been reduced. The IRS plans to document and quantify these benefits to ensure decisions made about the future of Direct File are data-driven and based on a comprehensive analysis of both costs and benefits along with other relevant considerations.

RECOMMENDATION 3

The Commissioner of Internal Revenue should use the cost and benefit data collected during the pilot along with other relevant considerations to inform future decisions about the Direct File system.

COMMENT

The IRS agrees with this recommendation. The Commissioner will use the cost and benefit data collected during the pilot along with other relevant considerations to inform future decisions about Direct File.