Preying Preparers:
How Storefront Tax Preparation Companies Target Low-Income Black and Brown Communities

By: Portia Allen-Kyle, Color Of Change, and Better IRS staff
INTRODUCTION

Approximately 150 million tax returns are filed with the Internal Revenue Service (IRS) each year. For more than half of these returns, American taxpayers rely on — and pay — tax preparation professionals. The $10 billion tax preparation industry is lucrative and ubiquitous. Lacking federal oversight, many of the more than 700,000 tax preparers in the United States are, at best, unqualified and, at worst, purposely taking advantage of taxpayers, are committing fraud, and engaging in misconduct. Previous research has established that storefront tax preparation operations that employ these corrupt or unqualified preparers concentrate in low-income communities to exploit the most vulnerable taxpayers. To build upon that research, we find that for-profit tax preparation companies are more prevalent in Black and Brown communities. This report reviews how unregulated tax preparers take advantage of tax filers, especially low-income Black and Brown Americans. We conclude with recommendations for policymakers to protect taxpayers by regulating the tax preparation industry and implementing policies that ensure our tax system works for everyone.
Most Tax Preparers Are Unqualified to Assist Tax Filers with Their Returns

The IRS’ National Taxpayer Advocate has referred to the $10 billion tax preparation industry as “the wild, wild West.” Due to a lack of federal oversight, there is significant and unprecedented risk for abuse and poor quality of service by tax preparation “professionals.” This lack of regulation allows these companies to exploit taxpayers who are simply seeking an easy solution to filing their taxes in an intentionally difficult system.

There are several types of tax preparers. Some (e.g., attorneys, Certified Public Accountants, and Enrolled Agents) are required to demonstrate key competencies and proficiencies and to comply with continuing education requirements. Others, called unenrolled preparers, prepare and sign taxpayers’ returns, but there are no federal requirements for them to demonstrate any knowledge of tax laws or regulations or obtain any credentials. Fifty-five percent of tax preparers1 fall into this second category, and they prepare more than 25 percent of all returns. Most of these unenrolled preparers are employed by large storefront tax preparation chains, such as H&R Block, Jackson Hewitt and Liberty Tax Service. Only seven states2 impose minimum competency standards for unenrolled preparers.

Unenrolled preparers often lack any training in tax rules and regularly commit both intentional and unintentional errors on tax returns. For example, one Government Accountability Office (GAO) study found that only approximately 10 percent3 of preparers at large tax preparation chains correctly calculated tax refunds. These mistakes resulted in a range of errors, shortchanging taxpayers by as much as $52 and giving erroneously large refunds by as much as $3,718.

---

1 California, Connecticut, Illinois, Maryland, Nevada, New York, and Oregon

---

I was young at my first job, and I never filed taxes before. I was scared and had no experience with money. I didn’t even have a checking account. I went to H&R Block. An older man was doing my taxes and had gotten my Social Security number wrong. I had him correct it. He was irritated at me for delaying him. He did not ask me questions; I handed him my W-2 and driver’s license. He only spoke to me to ask for those two items.

The following year, I began dating an accountant. He asked where I did my taxes. He asked me why I didn’t claim the Earned Income Tax Credit (EITC). I asked, what is that? I let him look at my 1040, and he amended my taxes. I didn’t know what I didn’t know. I went to a business that just saw me as a number.

- Teresa
Former H&R Block Customer
Edited for clarity
These unqualified preparers continue to submit returns and charge taxpayers for their services. The GAO estimates that 60 percent of returns submitted by paid preparers contain errors. These mistakes — intentional or not — can cause great harm to Americans, exposing them to potential fines if refunds are larger than they should be or causing financial insecurity if refunds are incorrectly small.

When tax preparers falsely claim deductions or credits, it increases the likelihood of taxpayers being audited. IRS records show that more than 112,000 people have reported fraud or misconduct by their tax preparers during the past decade, including preparers making up dependents that did not exist, faking W-2s and other documents to increase refunds and editing returns without the taxpayer’s consent. Audits are expensive and stressful, and many people are unaware that the conduct of their tax preparers can increase their audit risk.

When the IRS attempted to regulate paid preparers in 2010, roughly 1 in 4 of the 84,000 unenrolled preparers who took the competency exam failed and more than 320,000 others never took it.

In 2008, the U.S. Treasury Department’s inspector general for tax administration had auditors pose as taxpayers and paid to have tax returns prepared by unenrolled preparers at large, commercial preparation chains and small, independently owned preparation practices. Their results are striking: 61 percent of the returns were prepared incorrectly, and 35 percent of the inaccurate returns contained willful or reckless misstatements or omissions. In 2009, the acting commissioner of the New York Department of Taxation and Finance testified at an IRS public forum about a 20-month effort to investigate unscrupulous tax preparers and described investigators' findings as “an epidemic of unethical and criminal behavior.” The department made at least 20 arrests after finding a fraud rate of nearly 40 percent.

Taxpayers are largely unaware that unenrolled preparers are unregulated and unqualified. Many taxpayers often incorrectly believe they are engaging directly with an accountant. A 2017 poll conducted by the Consumer Federation of America found that 68 percent of respondents believe there are state or federal licensure requirements for paid preparers.
Unregulated Tax Preparers Consistently Take Advantage of Low-Income Taxpayers and Reduce the Economic Impacts of Tax Credits for Low-Income Families

Unenrolled preparers submit 75 percent\(^7\) of all returns that claim the Earned Income Tax Credit (EITC), a federal tax credit that boosts the income and eases the economic burdens of 23 million\(^8\) low- and moderate-income families. The EITC, averaging about $2,500, lifts about 6 million\(^9\) people out of poverty each year and reduces income inequality between Black and white households by 5 percent to 10 percent.\(^{20}\)

Tax preparation chains target impoverished communities by clustering in areas with the most EITC claimants. A 2016 Progressive Policy Institute (PPI) study found that ZIP codes with the highest level of EITC filers have 75 percent\(^1\) more tax preparers per filer than those with moderate amounts of EITC filers. Preying on EITC-eligible taxpayers is just one example of the industry’s predatory business practices.

While these unscrupulous tax preparers make mistakes across the board, error rates for EITC beneficiaries are particularly high. GAO studies have found error rates for EITC tax returns filed by paid tax preparers ranging as high as 94 percent.\(^{21}\)

*The PPI study defines “high-EITC” ZIP codes as those with a majority of filers claiming the EITC and “moderate EITC” ZIP codes as those with between 10 percent and 40 percent of filers claiming the EITC.

**EARNED INCOME TAX CREDIT RETURNS FILED BY PROFESSION (TAX YEAR 2018)**

<table>
<thead>
<tr>
<th>Profession</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unenrolled Preparer</td>
<td>75.1%</td>
</tr>
<tr>
<td>Certified Public Accountant</td>
<td>9.4%</td>
</tr>
<tr>
<td>Enrolled Agent</td>
<td>8.5%</td>
</tr>
<tr>
<td>State-Regulated Tax Preparer</td>
<td>5.7%</td>
</tr>
<tr>
<td>Certified Acceptance Agent</td>
<td>0.9%</td>
</tr>
<tr>
<td>Attorney</td>
<td>0.4%</td>
</tr>
<tr>
<td>Enrolled Actuary</td>
<td>0.0%</td>
</tr>
<tr>
<td>Enrolled Retirement Plan Agent</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

Taxpayers eligible for the EITC spend a considerable amount of their refunds on filing their taxes. In 2016, PPI found that it cost low-income taxpayers in Washington, D.C. and Baltimore, Maryland as much as 22 percent of their average EITC refunds (about $400, or $513 in today's dollars) to file their taxes. Again, this is not a new problem. In 2002, a Brookings study found that tax preparers charged EITC claimants fees amounting to more than 10 percent of their refund, roughly $114 ($195 in today's dollars), for the preparation and electronic filing of a federal and state return.

Between high costs of preparation services and extensive mistakes, the impact of EITC credits are blunted for many of its claimants.

**Tax Preparers Target Low-Income, Black and Brown Communities**

Building off of the 2016 PPI study, we analyzed how tax preparation chains cluster in areas with the highest shares of low-income and Black and Brown taxpayers.* We find that counties with more Black taxpayers and EITC claimants have 7 percent more Liberty Tax and 14 percent more Jackson Hewitt locations. Counties with more Hispanic taxpayers and EITC claimants have 11 percent more Liberty Tax locations, 8 percent more Jackson Hewitt locations and 5 percent more H&R Block locations.

Their preying on EITC claimants is not by accident or coincidence; exploiting low-income taxpayers is core to the business model of these companies. Given the eligibility requirements for the EITC, these taxpayers often are in economically precarious positions and can fall prey to unscrupulous practices such as payday lending products that advance claimants their tax refund if they agree to let the tax preparation company skim off the top.

Preparers often offer low-income tax filers advances on their refunds, called refund anticipation checks (RACs). Preparers charge taxpayers as much as $60 for advances on federal refunds and $10 for state refunds. In 2015, 19 million taxpayers, including more than 10 million EITC claimants, received a RAC for a total cost of about $475 million. In some cases, tax preparers offer refund anticipation loans (RALs), often with high fees and interest. Refund anticipation loans are used more commonly by Black taxpayers. Black households are 36 percent more likely to use return advance products than white households.

H&R Block and Jackson Hewitt both offer refund advance loan products with interest rates ranging upwards of 33 percent. To lure taxpayers in, they advertise zero-percent interest rates that require the filer to have their taxes prepared by the corporation. In actuality, the cost of the loan is built into the high cost of the tax preparation services.

---

* For a description of data sources and methodology, see the appendix.

---

"Worst of all was the upselling. We never advertised how much our prep fees were, claiming that we could only know once we had gone through the prep work to understand what forms were needed. While true, we could have listed the costs for such forms. However, those high prices would have deterred people from coming to us in the first place. I regularly prepared returns from $200-$500 before additional services and products, and I wasn’t even an advanced preparer. After I put everything into the system and the figures were final, only then would a customer know how much they owed, and at that point, many were so tired and ready to get it over with that they would succumb to paying the fees.

Steven H., Former H&R Block Tax Preparer"
Beyond incompetence or willful fraud, tax preparers take advantage of low-income taxpayers through aggressive and deceptive marketing practices. For example, a recent suit brought against Liberty Tax by the D.C. Attorney General alleges that the chain “aggressively markets its services to low-income residents by offering them $50 in cash ‘just for filing,’ but then secretly increases the cost of tax preparation for individuals who accept the cash payment.” On average, Liberty Tax’s predatory pricing scheme results in consumers being charged between $67 to $200 more for tax preparation services than those who do not participate in the promotion. EITC filers who claimed the promotion were charged an average of $93 more.

H&R Block is predatory and frequently targets the poorest communities with their “additional products,” knowing that the average person does not have $200-$500 to pay for a return up front. So, the company charges customers additional fees (on top of the original filing costs) to pay later, and H&R Block takes their money from the customer’s return. Or worse, H&R Block has a system that has nothing to do with tax returns. It’s just loans for a theoretical return amount. You can apply for a loan, and whenever you get your tax return, you can repay the loan you took out. That puts the customer on the hook for returning to the company to prepare their taxes, hoping their return covers the loan and the service fee. The tax prep industry is disgusting.

Steven H.,
Former H&R Block Tax Preparer

Past Federal Attempts to Regulate Preparers Have Failed, Though Limited State Efforts Have Proven Successful

The federal government has recognized the need for regulation of and minimum standards for tax preparers since at least 2002. The Taxpayer Advocate Service’s Annual Report to Congress in 2002 noted, “Taxpayers would be better served, and compliance would likely be improved, if tax preparers were required to meet minimum standards of competency.” Since then, similar recommendations have been made in at least eight of the Service’s annual reports. Over the past two decades, the tax preparation industry has staunchly opposed regulation and oversight, spending millions of dollars lobbying against regulations and consumer protections that would threaten its business model that relies on the exploitation of unsuspecting customers.

In 2011, the IRS introduced the Registered Tax Return Preparer Program, finally establishing rules for tax preparers, including a competency exam and continuing education requirements. In 2014, Loving v. IRS, an opinion written by now-U.S. Supreme Court Justice Brett Kavanaugh, held that the 2011 regulations were invalid because they extended to unenrolled preparers, which the D.C. Circuit Court found to be outside of the scope of IRS jurisdiction. As a result, regulation of these preparers has largely been left to the states.

As mentioned before, prior to the 2014 opinion in Loving, the IRS found that roughly 1 in 4 of the 84,000 unenrolled preparers who took the competency test failed and more than 320,000 others never took it. Further, IRS education and compliance actions for noncompliant preparers have declined in recent years, from nearly 25,000 preparers in FY2017 to 13,000 in FY2021. This decrease in enforcement actions against preparers enables greater harm to taxpayers.

Currently, only California, Connecticut, Illinois, Maryland, Nevada, New York, and Oregon regulate paid preparers. Oregon, for example, has minimum age, education and tax competency requirements for licensed tax preparers. California has professional education and registration requirements. In 2008 GAO found that the odds of a return being accurately filed by a tax preparer in Oregon were 72 percent more likely than a comparable return in the rest of the country.
Considerations for Policymakers

Americans overwhelmingly support regulating tax preparers and taking on the tax preparation industry. In 2009, the IRS solicited comments from the public regarding the regulation of tax preparers. Of more than 500 comments received, minimum education or testing requirements and increased oversight and enforcement were common themes.

86% of Americans support requiring paid tax preparers to pass a competency exam.

88% of Americans support licensing requirements by an agency that would also resolve complaints and enforce consumer protections.

76% of Americans support the development of a free IRS-run tax prep option. Support is higher among filers who earn less than $50,000 (77%) and who are Black (80%).

To protect American taxpayers, especially low-income families and communities of color, policymakers should:

Regulate all paid preparers, not just enrolled agents.

Given the extent of incompetence and fraud among unenrolled preparers, the IRS should require that any paid preparer demonstrate minimum competencies and be held accountable for gross misconduct. While this may require new legislation, some legal experts argue that the IRS can challenge the Loving precedent. The Biden administration should explore all legal avenues to more aggressively regulate unscrupulous preparers, including preventing unenrolled preparers from preparing tax returns for compensation and publicly disclosing sanctions imposed on offenders.

Aggressively defend and expeditiously expand Direct File, the IRS’ free option for taxpayers to file using the IRS’ own filing software.

As a result of the Inflation Reduction Act, the IRS launched a Direct File pilot program after a more than two-decades-long effort for the federal government to offer a free, digital tax filing service. The pilot currently is available to tax filers with simple returns in 12 states, including filers who claim the EITC and Child Tax Credit. Currently, roughly 1 in 5 eligible families don’t get their EITC because it’s too hard or expensive to file taxes. A Direct File system will empower taxpayers to more easily access these essential benefits. However, there have been widespread bad-faith attacks on the program due to intense lobbying from the tax preparation industry. Direct File will save taxpayers money, increase access to tax credits that benefit low-income families and eliminate taxpayers’ reliance on paid tax preparers.

Invest in the Volunteer Income Tax Assistance (VITA) program.

The VITA program provides grants to community organizations to provide free tax preparation services to low- and moderate-income individuals, people with disabilities, seniors and limited English speakers. Many VITA sites offer wraparound services to remove barriers for taxpayers, including by offering interpreters, child care, evening and weekend hours, and accommodations for people with disabilities. Further, the IRS certifies tax preparers at VITA sites, and all tax returns are reviewed by at least one other preparer before they’re submitted. As a result, accuracy rates are above 97 percent. VITA centers can help increase the uptake of the EITC and other tax credits that low-income taxpayers often don’t know they are eligible for.
Appendix: Data and Methodology

We identify the location of each storefront preparer using the Authorized IRS e-file Provider database, which is a nationwide listing of all businesses that participate in the IRS e-file program.\(^4\) Using the Wayback Machine, we are able to access this database as of September 2020, capturing the providers for tax year 2019 to match the demographic data and account for any COVID-related preparer closures. One limitation of the database is that providers must opt-in to be listed in the locator service when they apply to participate in the e-file program. Of course, this means that not all providers will choose to be listed. However, we assume that the vast majority of providers opt-in so that they can benefit from being listed on the IRS’ e-File Provider Search Tool that allows taxpayers to find preparers in their area.

This database contains the name (e.g., H&R Block) and address of each preparer. Because ZIP codes are not particularly statistically meaningful, and in dense areas, it’s very likely that taxpayers would live in one ZIP code and travel a short distance to a tax preparer in another ZIP code, we use counties. \(^*\) For example, in Dallas County, Texas, there are 164 ZIP codes, including 15 that extend into adjacent counties. We allocate tax preparers proportionally when ZIP codes cross county lines. \(^**\)

Using the IRS Statistics of Income report, we collect the number of taxpayers in each county who claim the EITC; the number of taxpayers who use a paid preparer; and the number of taxpayers who utilize tax preparation services through the VITA program. We use tax year 2019 data to account for any data irregularities during COVID-19 pandemic years and to match the available demographic data from the Census. We compute the share of taxpayers who claim the EITC not as a proxy for income — given that the lowest income taxpayers are unlikely to qualify — but because previous research shows that storefront tax preparers exploit EITC-eligible taxpayers.

To collect demographic information for county populations, we use the American Community Survey 5-year estimates spanning 2016-2020. We compute the share of the population in each county that is white, Black and Hispanic. For our analysis, we categorize counties into above and below national average shares of each race.

Using a logistic regression, we model the correlation between demographic variables (race and EITC) and the number of large chain tax preparation locations, controlling for population.

Testimonials: For this report, Color Of Change collected personal stories from individuals subscribed to its email list on January 26, 2024.

\(*\) This is different from the PPI study and an early Brookings study that uses the same methodology, in that they compute and compare the number of tax filers per preparer within a ZIP code. We believe that this county-level analysis more accurately captures the realities of where taxpayers are likely to commute.

\(**\) For example, if there are two tax preparers in a ZIP code that is 60 percent contained within county X, and 40 percent contained within bordering county Y, 1.2 preparers would be allocated to county X and 0.8 to county Y.
References


3 ibid


5 ibid


12 ibid


14 ibid


Preying Preparers: How Storefront Tax Preparation Companies Target Low-Income Black and Brown Communities


22 ibid

23 ibid


References


35 ibid


