

The IRS's Free Direct Filing Pilot Program

Updated February 7, 2024

Individuals may satisfy their income tax obligations by filing a paper return or filing an electronic one (e-filing). To e-file, a taxpayer must use software preapproved by the Internal Revenue Service (IRS). Most individual returns are e-filed. [For the 2022 tax year \(through December 29, 2023\)](#), the IRS received 162 million returns, 93% of which (150 million) had been e-filed. Professional preparers submitted 57% of the e-filed returns and self-preparing individuals the other 43%.

Historically, the IRS has provided taxpayers with [several options](#) for free e-filing, but those options did not include e-filing directly with the IRS through a secure portal on its website, an option known as Direct File (DF). As a result of several recent developments, a DF option is now available as a pilot program during the 2024 filing season.

This Insight describes how the pilot DF system came to be and how it is intended to work.

Emergence of An IRS Direct-File Option

The IRS's efforts to create a DF system go back to the early 2000s. The initial attempt was a response to a 2001 directive from the [Office of Management and Budget](#) to expand e-filing as part of an effort to increase the range of online federal government services. In 2002, concerned about the cost of developing and maintaining a DF system and facing opposition in Congress to such an initiative, the IRS formed a partnership with a number of commercial tax preparation firms to provide free tax preparation and e-filing to lower-income taxpayers through a program known as Free File. Under the agreement establishing the program, member companies were to provide free e-filing to eligible taxpayers through their online platforms, and in return, the IRS would refrain from developing its own DF system.

This restriction lasted from 2003 until 2019, when it was dropped from the memorandum of understanding governing the Free File program. There were several reasons for this decision. Historic usage rates for the program had ranged from 3% to 4% of eligible taxpayers. The IRS invested little in promoting and policing the program. Some media reports in 2019 revealed that some member companies had been diverting Free File-eligible taxpayers to the companies' paid filing services.

Interest in the IRS providing a DF service seems to have grown since 2019. The Inflation Reduction Act (IRA, P.L. 117-169) provided the IRS with \$15 million to create a direct e-file task force and deliver two reports to Congress by May 16, 2023. The task force was to prepare one report, and an "independent third party" chosen by the IRS was to prepare a second report.

Congressional Research Service

<https://crsreports.congress.gov>

IN12270

IRS Report

The IRS [report](#) addressed two topics: (1) taxpayer “opinions, expectations, and level of trust” for an IRS-run DF system and (2) the cost of developing and operating such a system under different levels of taxpayer income and tax complexity.

To assess taxpayer attitudes toward a “hypothetical free IRS-provided online tool,” the IRS task force reviewed the results of two recent surveys and interviewed 14 taxpayers about their experiences using an IRS prototype of a DF system. The survey results indicated that over 70% of taxpayers would be “very or somewhat interested” in using a free IRS-run online filing tool. The task force also found that taxpayer interest in such a tool depended on (1) the percentage of taxpayers who regard the IRS as a legitimate provider of such a service; (2) the availability of concurrent filing for federal and state income tax returns; and (3) the advantages of using an IRS filing tool relative to other filing options, such as faster refunds, prefiled filing, and a reduced audit risk.

The IRS report noted that the cost of developing and updating a DF system would be driven by three factors: (1) critical software and equipment; (2) system maintenance and updating; and (3) customer support. It also provided cost estimates for three filing scenarios: 5 million filers, 10 million filers, and 25 million filers under both a simple tax situation and a more complex one. The results indicated that the annual cost of developing and operating a DF tool rose in step with the number of filers, but the cost per filer fell as the number of filers rose. For instance, the cost per return under a simple tax situation was about \$13 with 5 million filers but dropped to \$9 with 25 million filers.

Independent Third-Party Report

The independent third-party [report](#) assessed the “the overall feasibility approach, schedule, cost, organizational design” of an IRS DF system, and the Internal Revenue Service capacity to deliver one.

According to the report, the feasibility and success of a DF system depended on six factors:

- continuous IRS managerial support;
- gradual and flexible system development;
- sustained funding that allows for continued upgrades in the system’s hardware and software;
- concurrent e-filing for federal and state income tax returns;
- accurate, timely, and reliable customer service; and
- secure protection of taxpayer information in a DF system.

The third-party report estimated the annual cost of a DF option using the same cost factors as the IRS report. It provided cost estimates for five filing scenarios (1 million users, 2 million users, 5 million users, 10 million users, and 25 million users) under a range of uncertainty about a DF system’s long-term costs. In line with the IRS report, the results showed that the overall cost rose and the per-return cost fell as the total number of filers expanded.

Current Status of the IRS’s Pilot Direct-File Program

On January 25, 2024, the IRS opened its pilot DF program for limited use during the 2024 filing season. A main aim of this effort is to assess the technical feasibility, cost, and taxpayer response to a DF system as another free e-filing option for taxpayers with relatively simple tax situations. The pilot DF is being phased in. Initially, only federal and state government employees residing in Alaska, Arizona, California, Florida, Massachusetts, Nevada, New Hampshire, New York, South Dakota, Tennessee, Texas,

Washington, and Wyoming may file through the DF pilot. More taxpayers may become eligible to file through the pilot as the 2024 filing season progresses.

At the moment, [only certain tax items](#) can be reported through the pilot DF program. Income reporting is limited to W-2 wages, Social Security and railroad retirement income, unemployment compensation, and interest of \$1,500 or less. Three credits may be claimed: the Earned Income Tax Credit, the Child Tax Credit, and the Credit for Dependents. Users may claim three deductions only: the standard deduction, student loan interest, and educator expenses.

Author Information

Gary Guenther
Analyst in Public Finance

Disclaimer

This document was prepared by the Congressional Research Service (CRS). CRS serves as nonpartisan shared staff to congressional committees and Members of Congress. It operates solely at the behest of and under the direction of Congress. Information in a CRS Report should not be relied upon for purposes other than public understanding of information that has been provided by CRS to Members of Congress in connection with CRS's institutional role. CRS Reports, as a work of the United States Government, are not subject to copyright protection in the United States. Any CRS Report may be reproduced and distributed in its entirety without permission from CRS. However, as a CRS Report may include copyrighted images or material from a third party, you may need to obtain the permission of the copyright holder if you wish to copy or otherwise use copyrighted material.