

States Allowing Income Tax “Return-Free Filing”

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Issue

Identify the states that implement “return-free filing” and determine if this method reduces processing and other administrative costs.

Summary

California appears to be the only state that implements return-free filing, according to the Federation of Tax Administrators and the National Conference of State Legislatures. In a return-free filing system, the state’s tax agency (1) calculates taxpayers’ income tax liability based on the wage and interest income data it receives from employers and financial institutions, respectively; (2) prepares the returns; and (3) sends them to the taxpayers to review and, if necessary, amend. Taxpayers decide whether to submit these returns or prepare and submit their own.

California’s return-free filing program (i.e., [ReadyReturn](#)) has these features, but is available only to taxpayers who had previously submitted simple, uncomplicated returns and subsequently choose to file the state-prepared returns. The California Franchise Tax Board (CFTB), which collects state personal and corporation income taxes, advertises the program and prepares the returns for eligible taxpayers

States That Have Experimented with Return-Free Filing

In the mid-1990s, Michigan offered return-free filing to taxpayers with less than \$100 in investment income, but dropped the program after few taxpayers filed such returns. Louisiana enacted a similar program, but did not implement it because of Y2K-related computer problems (that were eventually resolved) ([Policy Analysis of Return Free Tax System](#)). Lastly, in 2007, Minnesota considered but did not enact a [bill](#) requiring the tax agency to develop a return-free filing program.

who request them. CFTB stated that it processed about 75,000 ReadyReturns in 2014 ([Pivoting Away from Paper](#), CFTB, May 13, 2014).

It appears that CFTB's most recent [cost savings analysis](#) for the ReadyReturn program is for FY 2011. CFTB estimated that it would cost an average of 34 cents to process a ReadyReturn, compared to an average of \$2.59 to process a conventionally prepared return, a difference of \$2.25 per return. Projecting 160,000 potential ReadyReturns for FY 11, CFTB estimated the program would save about \$235,000, after netting \$125,000 in operating costs.

California's ReadyReturn Program

Pilot

CFTB piloted the ReadyReturn program in 2004 and 2005, targeting about 50,000 resident taxpayers who submitted "simple returns" in the 2003 and 2004 tax years, respectively. For the pilot's first year, a taxpayer qualified for a ReadyReturn if he or she:

1. used the single filing status,
2. received wage income from only one employer,
3. claimed the standard deduction,
4. claimed no dependents, and
5. was not claimed as a dependent on another's return.

For the 2005 tax year, CFTB modified the program's eligibility criteria. Among other things, it extended eligibility to taxpayers who filed simple returns in 2004 and:

1. whose total wages did not exceed the itemized deduction phase-out and
2. had income indicating a filing requirement or a refund ([Your California ReadyReturn: ready and waiting for you](#)).

CFTB invited eligible taxpayers to participate in the program, sending them their ReadyReturns and instructions on how to submit them. About 11,000 taxpayers submitted ReadyReturns in 2004, and 10,000 in 2005. In response to a 2006 CFTB [survey](#), most ReadyReturn filers reported that it took less time to review and submit a ReadyReturn than it did to prepare and submit a conventional one ([Ready Return Pilot: Tax Year 2004 Study Results](#)).

Full Implementation

CFTB began fully implementing the program in 2007 using generally the pilot program's eligibility criteria. In 2009, it extended eligibility to almost 2 million more taxpayers who had in the prior year:

1. filed as head of households,
2. no more than five dependents, and
3. claimed only the renter's tax credit.

In its 2009 report to the legislature, CFTB estimated that it would cost 34 cents to process the average ReadyReturn in FYs 10 and 11 compared to \$2.59 for a conventional return. As Table 1 shows, CFTB projected that total net cost savings would increase as the number of ReadyReturn filers increased and more did so using the state’s electronic filing system.

Table 1: Projected Net Savings to State Due to ReadyReturns, FY 2010-2011

Net Cost Savings Calculation	Fiscal Year	
	2010	2011
Projected Number of Eligible Ready Returns	90,000	160,000
Cost to Process if Filed on Paper (\$ 2.59 per return)	\$233,100	\$414,400
Cost to Process ReadyReturns (\$0.34 per return)	\$30,600	\$54,400
Estimated Cost Savings/Avoidance*	\$202,500	\$360,000
Projected ReadyReturn Maintenance Costs	\$125,000	\$125,000
Net Savings to State Due to ReadyReturns	\$77,500	\$235,000

* The report did not define “avoidance,” but a 2001 [Fraser Institute-commissioned study](#) suggests that the term refers to the savings generated by an increase in error-free returns.

Source: [ReadyReturn: Franchise Tax Board Report to the Legislature](#) (April 23, 2009, p.4)

Hyperlinks

CFTB Reports

[Franchise Tax Board Report to the Legislature: ReadyReturn](#), CFTB, April 23, 2009

[Pivoting Away from Paper](#), CFTB, Internal Revenue Service Oversight Board Public Forum, May 13, 2014

[Ready Return Pilot: Tax Year 2004 Study Results](#), CFTB, April 2006

[ReadyReturn: Your California tax return ready and waiting for you.](#) CFTB (undated)

State Reports

[Analysis of SF 665 \(Rest\) and HF 843 \(Benson\)](#), Minnesota Department of Revenue (March 2, 2007)

Other Studies

[Policy Analysis of “Return-Free” Tax System](#), Boisture, Lauber, and Paz, April 2006, commissioned by the Computer and Communications Industry Association

[Pre-Completed Income Tax Returns: Evidence from the California ReadyReturn Program](#), Erard, 2011, commissioned for the Fraser Institute

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