Consumer Federation of America

NATIONAL CONSUMER LAW CENTER INC

<u>For Immediate Release</u>
January 31, 2002

Contact: Jack Gillis, CFA, 202-737-0766
Jean Ann Fox, CFA, 757-867-7523
Margot Saunders, NCLC, 202-986-6060

TAX LOANS SKIM HUNDREDS OF MILLIONS FROM WORKING POOR

Washington, DC – As tax season kicks into high gear, two leading consumer groups issued a comprehensive report warning about high cost, high interest tax refund loans. Fast tax refund loans cost borrowers from $29 to $89 for loans that last about ten days, resulting in annual interest rates of 67% to 774%, according to a new report issued by Consumer Federation of America and the National Consumer Law Center.

"Cash-strapped consumers will pay about $800 million in RAL finance charges alone to borrow their own money," Jean Ann Fox, director of consumer protection for CFA, stated. "Refund anticipation loans are extremely expensive, similar to payday loans, rent to own, car title pawns, and other forms of fringe credit."

Using names such as SuperFast Cash, Instant Money, Fast Cash Refunds, tax refund anticipation loans (RALs) are short-term loans secured by the consumer's expected refund. About 11 million consumers gets RALs, with 4.5 million RALs made by H & R Block, the single largest tax preparer in the nation.

The loans are repaid when the consumer's refund is received in a temporary bank account set up by the lender. Unfortunately, consumers often do not realize that RALs are loans, and that they are obligated to repay them even if tax refunds are disallowed or less than expected.

The CFA/NCLC report, "Tax Preparers Peddle High Priced Tax Refund Loans: Millions Skimmed from the Working Poor and the U. S. Treasury," also documents the impact of RALs on the working poor who qualify for the largest federal anti-poverty program, Earned Income Tax Credits. EITC benefits are delivered as a lump sum through the tax refund system with about $30 billion provided to 18.4 million low-income taxpayers last year.

"The EITC lifts almost five million people, over half of them children, out of poverty," Margot Saunders, NCLC managing attorney, stated. "EITC recipients need every penny of those benefits to build assets, pay necessary bills, and make ends meet in this economy."

Why EITC Recipients Get Tax Loans

The report reveals that forty percent of taxpayers who get refund anticipation loans are EITC recipients. It also discusses the reasons for why EITC recipients get RALs, including the scarcity of free tax preparation assistance and the fact that the working poor often do not have the cash up front to pay commercial tax preparation fees.

Almost a Billion Dollars of EITC Benefits Go to Tax Prep, Loans, and Fees

CFA and NCLC estimate that tax refund loans siphon off an estimated $324 million in loan fees and an additional $670 million in tax preparation fees, electronic filing fees, and check cashing fees every year from EITC recipients who get RALs. The total bill for the typical taxpayer is $267, while a total of $994 million is drained from the Earned Income Tax Credit program.

Type of Fee	**Cost to Taxpayer**	**Drain on EITC Program**
RAL loan fee	$75	$324 million
Electronic filing fee	$40	$172.8 million
Check cashing fee	$67	$130 million
Tax preparation fee	$85	$367.2 million
Total	**$267**	**$994 million**

"Taxpayer benefits for the working poor belong in consumers' pockets, not in the coffers of tax preparation firms and their partner banks," Jean Ann Fox stated. "Holes in the consumer protection safety net permit usurious lending, deceptive marketing of loans, and unfair collection tactics."

Holes in the Consumer Protection Safety Net Harm Taxpayers

The report discusses the lack of regulation for RALs by both the federal government and the states, including the fact that RALs evade state loan laws and usury caps using loopholes created by federal law. CFA and NCLC recommend that refund anticipation loans should be banned outright or made subject to state usury and small loan interest rate laws. Tax preparation services should not be permitted to evade state consumer protections by partnering with national banks to make triple digit interest loans.

"The IRS is under pressure from Congress to meet a goal of having 80% of tax returns filed electronically by 2007," Margot Saunders noted. "The IRS is not likely to interfere with commercial tax preparers who boost e-filing through refund loans. The IRS even made RALs less risky for lenders in 1999."

The IRS reinstated the Debt Indicator service to screen for any claims against consumers' refunds. Although fees were expected to drop as a result of the Debt Indicator service, H & R Block's fees in 2001 were back up to pre-Debt Indicator levels, with revenue up by 49% from 2000 to 2001. Per-RAL revenue rose by 44% while sales volume only increased by 2.7%, indicating that most of the Block revenue jump came from higher finance charges.

RAL Users are Vulnerable Consumers

The report notes that RAL customers tend to have $10,000 to $15,000 annual incomes, are unemployed or employed in service occupations, and possess less than a high school education. An industry marketing study found that customers who used the "Rapid Refund" service were frequently in dire straits and used RALs to get cash for pressing needs. Taxpayers whose income is so low as to be eligible for the Earned Income Tax Credit are a captive market for return preparers.

Low Income Consumers Need Bank Accounts to Speed Up Refunds

NCLC and CFA recommend that the First Accounts pilot projects funded by Congress to provide electronic bank accounts to unbanked consumers who do not receive ongoing federal benefits should be targeted at working low-income consumers eligible for the EITC.

"Ten million families do not have bank accounts. Without bank accounts, cash-strapped consumers cannot receive speedy refunds that are electronically deposited," Margot Saunders said. "The Treasury should encourage banks to allow Electronic Transaction Accounts for federal benefits recipients to receive tax refunds so that consumers can get refunds quickly without borrowing."

Deceptive Advertising and Marketing of RALs

The report details the long history of deceptive advertising complaints about refund anticipation loans. As early as the mid-1970's, the Federal Trade Commission ordered one lender to stop advertising its RAL as an "instant tax refund." State attorneys general followed up with cases against deceptive advertising of RALs as refunds. In 2001 the New York City Department of Consumer Affairs cited H & R Block for 2,230 violations of the city's consumer protection law for misrepresenting its Rapid Refunds, the sixth case brought by New York City against the company.

NCLC and CFA recommend that the IRS enforce its advertising rules for refund anticipation loans by revoking the electronic filing privileges of commercial tax preparation companies that violate them. The IRS should refer bank partners of offending tax preparers to the Office of the Comptroller of Currency or other appropriate agency for enforcement.

"Everyone wants a cut out of consumers' tax refunds, from tax preparers, to check cashers, to car dealers and retailers," Jean Ann Fox stated. "Consumers need help from free tax preparation services and protection from deceptive lenders in order to get back all of their tax refunds and EITC benefits."

###

CFA is a non-profit association of more than 285 groups, which, since 1968, has sought to advance the consumer interest through advocacy and education.

NCLC is a non-profit organization specializing in consumer issues on behalf of low-income people. NCLC works with thousands of legal services, government and private attorneys, as well as organizations, who represent low-income and elderly individuals on consumer issues.

Report is available at www.consumerfed.org and at www.nclc.org. Printed copies are available for $30 from CFA, 1424 16th NW Suite 604, Washington, DC 20036.