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Consumer Federation of America

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ONE LAST BITE: FINAL YEAR FOR BANK TAX REFUND ANTICIPATION LOANS
Consumer Advocates Recommend Cheaper Alternatives for Getting Refund Fast

BOSTON, Mass.—A bright note for consumers as this tax season begins: This is the final year in which refund anticipation loans (RALs) will be available from banks on a large scale, nationwide basis. After this season, there will be an end to the hundreds of millions drained from taxpayer refunds by these high-cost, high-risk loans. “We will be glad to see the last of RALs, which were both high-cost and high-risk,” says Chi Chi Wu, staff attorney at the National Consumer Law Center (NCLC). “It’s not a moment too soon to stop multi-million dollar corporations from skimming off the tax refunds of hard-working families.”

Consumer advocates suggest that taxpayers looking for quick refund cash should consider these lower-cost or free alternatives

- Taxpayers with a bank account can get their tax refunds in 8 to 15 days with e-filing and direct deposit.
- Taxpayers without a bank account can get a fast refund by e-filing and having their refund deposited to a prepaid card, including any existing payroll or prepaid card that the taxpayer already has.
- H&R Block is even offering free refund anticipation checks (RACs) until early February if the customer uses its prepaid Block Emerald Card to receive the refund.

With RACs, the bank opens a temporary bank account into which the IRS direct deposits the refund check. After the refund is deposited, the bank issues the consumer a check or prepaid card and closes the temporary account. A RAC allows the consumer to pay for tax preparation fees out of the refund and provides the speed of direct deposit of tax refunds for unbanked taxpayers, but generally at an additional cost.

Life after Refund Anticipation Loans (RALs)

Even after the end of RALs, tax preparers and banks will continue to offer RACs, for which the banks generally charge about \$30 - \$32. Tax preparers may also charge their own “add-on” fees, which can range from \$25 to several hundred dollars. Since their main purposes is to defer payment of the tax preparation until the refund arrives, RACs may represent a high-cost loan of that fee. With the exception of free RACs, consumer advocates recommend taxpayers consider alternatives.

Prepaid cards are one alternative to allow taxpayers without a bank account to receive a fast refund. Taxpayers, however, should be cautious when selecting a prepaid card. “As with any financial product, taxpayers should compare costs and consumer protections,” recommends Wu.

Taxpayers without a bank account should also consider opening a bank account to receive their refund. “Getting a big refund is the perfect time to open a savings account and start a nest egg,” advises Jean Ann Fox, director of financial services for Consumer Federation of America.

Low-income taxpayers have a number of options for free tax preparation, including Volunteer Income Tax Assistance (VITA) (1-800-906-9887 or www.irs.gov) and AARP Tax-Aide sites (https://locator.aarp.org/vmis/sites/tax_aide_locator.jsp). Choosing a VITA or AARP Tax-Aide site saves taxpayers the cost of a tax preparation fee. Many VITA sites also offer services to help open a bank account or get a low-cost prepaid card, which enables taxpayers to get fast refunds without pay a fee. Free tax preparation may be available on bases, and since servicemembers are required to have bank accounts, they are able to benefit from the speed of electronic delivery of their tax refunds

There are also a number of websites that allow taxpayers to prepare and file their taxes online for free, such as the IRS Free File program (www.irs.gov) and the I-CAN! E-file site (www.icanefile.org).

Latest RAL Data

RALs are bank loans secured by the taxpayer’s expected refund—loans that last about 7 to 14 days until the actual IRS refund repays the loan. RALs are expensive. This year for Jackson Hewitt customers, Republic Bank is charging \$61.22 for a RAL of \$1,500, which translates into an APR of 149%. If the refund exceeds \$1561.22, the taxpayer is charged another \$29.95 when the remainder of the refund arrives in the form of a RAC, for a total of \$91.17 in fees. In fact, RALs are so expensive that the Military Lending Act bans them for servicemembers.

RALs were also big business. Using the most recent data available from the IRS, about 6.85 million taxpayers applied for a RAL in the 2010 tax filing season (for tax year 2009), and NCLC and CFA estimate that about 5 million received them. This represents a significant drop from the 8.4 million taxpayers who applied for RALs and the estimate of 7.2 million who received them in 2009. In contrast, the number of taxpayers receiving RACs has increased to an estimated 14.6 million taxpayers in 2010, up from the 12.9 million in 2009.

Last of the Banks Forced Out of RAL Lending in 2011

During the past few years, there have been a number of major developments in the RAL industry. The three biggest banks in RAL lending -JPMorgan Chase, HSBC and Santa Barbara Bank & Trust - left or were forced out of the business by December 2010. As a result of these actions, there were only three small, state-chartered banks making RALs in 2011— Republic Bank & Trust, River City Bank and Ohio Valley Bank, all based in Louisville, Kentucky.

In February 2011, the FDIC notified these banks that the practice of originating RALs without the benefit of the IRS Debt Indicator was unsafe and unsound. River City Bank and Ohio Valley Bank accepted the FDIC’s decision, but Republic Bank & Trust decided to fight. Republic appealed the decision to an administrative law judge, and sued the FDIC in federal court. In May 2011, the FDIC issued an “Amended Notice of Charges for an Order to Cease and Desist,” which detailed widespread legal violations in Republic’s RAL program and proposed a \$2 million civil penalty.

In December 2011, the FDIC reached a settlement with Republic in which the bank agreed to cease making RALs after April 2012, and to pay a \$900,000 civil penalty. Thus, after this tax season, there will be no banks left that make RALs.

Enter the Payday Lenders

With the end of RALs made by banks, a few high cost fringe lenders have stepped into the fray. Liberty Tax Service, which is planning an initial public offering, revealed in its prospectus that the tax preparation chain plans to partner with an unnamed non-bank lender to make RALs. Liberty’s website shows that it has partnered with SGS Credit Services, Inc., which appears to be linked with Texas payday lenders.

A prominent payday lender, Advance America, is offering “fast” refunds through its storefronts, although it is unclear whether the product is a RAL, a regular payday loan, or a RAC in actuality. The website for TaxWorks, a division of RedGear, which is owned by H&R Block, is promoting a “Tax Season Cash Advance” provided by Schear Lending Group and Atlas Financial Services. Schear Lending Group appears to be somehow affiliated with Ohio-based payday lenders.

“Consumers have even more reason to avoid RALs made by payday lenders,” advises Jean Ann Fox, “These RALs are likely to be more expensive and riskier.”

RALs made by nonbank lenders will most likely not be as widespread as bank RALs. Nonbank lenders do not have the legal ability, unlike banks, to flout state laws that cap interest rates, *i.e.*, usury laws. Tax-time loans from payday lenders and other storefront outlets that offer to prepare taxes and make loans may be subject to state loan laws, usury caps, or loan broker requirements in states that have them. Seventeen states (and District of Columbia) do not permit payday lending at all.

Upcoming Report Available in February 2012

NCLC and CFA will publish their annual comprehensive report on the RAL industry, regulation, and litigation in February 2012. The report will be available on NCLC’s website at www.nclc.org and on CFA’s website at www.consumerfed.org.

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National Consumer Law Center® 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.

The Consumer Federation of America is an association of nearly 300 nonprofit consumer groups that was established in 1968 to advance the consumer interest through research, advocacy and education.