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A closer look at tax refund loans

by Eddie Burkhalter
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The signs are everywhere. “Fast tax refunds”, “Quick cash” and “Instant refund”, but what is harder to see in the bright colors and glitter are hidden fees and the large interest rates required just to get a tax refund check as little as one week earlier.

Refund anticipation loans (RAL's) are a product of tax preparers whereby the preparer completes an applicants taxes, looks at paycheck stubs to estimate the person's expected tax refund, charges large fees and cuts the person a check – often on the same day. The preparer gets paid when the actual refund check is mailed from the IRS.

But with interest rates on those short-term loans from 50 to 500 percent, and a slew of additional “application,” “e-filing,” “processing” and “service” fees, these quick fixes often end up costing more than the flashy sign outside advertises.

And it is the kind of people these loans are targeted at, says Stephen Stetson – Policy Analyst for the Arise Citizens' Policy Project (ACPP), an Alabama non-profit that focuses on state policy decision that affect low-income persons, that makes them more akin to predatory lending like payday loans and title loans.

“They are almost exclusively used by people who can't afford them. The last thing we need in this economy is for folks to be hopping on the debt treadmill and not being able to get off,” said Stetson.

He urges people not to be tempted into paying to borrowing their own money for such little benefit. Instead, Stetson said there are other ways to receive that refund check earlier or get the funds that the over-prices loans would have provided.

Simply filing electronically can get that refund check in a week or two, he said, and although not always easy to find, some banks and credit unions still offer small loans. And there is always the old fashioned way to get through a rough patch – ask family and friends.

“The tough part about non-predatory loans for low-income folks, and this goes for payday and car title loans too, is access really does vary depending on where you live,” said Stetson. “Some banks and credit unions are just better than others at providing small loans to people with shaky credit.

“So it makes it tempting to go into that brightly-lit payday store or tax preparer and walk out with cash in your pocket. One of our real challenges as advocates is just educational. letting people know what loans exist in their communities. That's where the legitimate lenders can help their communities while building the wealth that results in customers for them down the road.”

How bad are RAL's for low-income people?

The National Consumer Law Center (NCLC), another non-profit that specializes in consumer issues affecting low-income people, reported that \$738 million in RAL fees and \$68 million in additional fees were paid by 8.4 million taxpayers in 2008. Fee's for these loans cost from about \$30 to more than \$125, according to NCLC.

There have been moves by federal regulators to stop, or at least lessen the availability of, these predatory loans. Beginning this year, tax preparers will not be able to use debt indicators (information provided by the IRS that let's tax preparers know if a person's refund might be funneled towards back child support, student loans or unpaid taxes). Without those debt indicators banks are less likely to back up these short term loans for preparers.

According to a Dec. 27 Reuters article, H&R Block, the nations largest tax preparation company, will no longer be able to offer RAL's. H&R Block's bank, HSBC, received notice from regulators at the Office of the Comptroller of Currency (OCC) to stop offering the loans to H&R Block customers. The tax preparer brought in about \$90 million from RAL's last year, according to the same article.

Others, such as the second largest U.S. tax preparer Jackson Hewitt, can still offer RAL's because their bank is regulated by the Federal Deposit Insurance Corp. and not the OCC.

H&R Block expressed concern over the move to prevent it from offering the loans while their competitors can continue their programs. In a Dec. 24 statement on H&R Block's website, company CPA and Community Manager Leigh Mutert wrote that "It strains the essence of free commerce when companies within one industry are held to different regulatory standards. The bottom line is that the regulatory and political challenges surrounding RALs were too steep to overcome. Know that we took every possible action, including a series of legal, political and business attempts, to overcome these challenges."

H&R Block will continue to offer Refund Anticipation Checks (RACs) that do not require out-of-pocket costs at the time the tax return is filed.

Stetson said that the recent regulations are a step in the right direction, but more needs to be done.

"Look, we all approve when the government steps in after a hurricane or disaster and tells merchants not to double the price of bread and gasoline and milk," he said.

"Why? Because we think it's wrong to take advantage of people that are desperate. These loans are the same thing. It's not right to stick it to somebody that needs money badly. And a loan that's loaded with fees and a triple-digit interest rate is the definition of the word "usury." We ought to be united as a state against taking advantage of folks."