Consumer Federation of America

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<u>For Immediate Release</u>

August 5, 2010

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Consumer Advocates Applaud End of IRS-Provided Service to Refund Anticipation Lenders

Washington, DC - Advocates at the Consumer Federation of America (CFA) and the National Consumer Law Center (NCLC) applauded today's announcement by the Internal Revenue Service that it will discontinue a service that aided banks in making high cost refund anticipation loans (RALs) to the working poor. The IRS has been providing a service called the "debt indicator" which helps banks that partner with tax preparers to make loans based on the borrower's expected tax refund. The "debt indicator" acts as a form of credit check, telling tax preparers whether a taxpayer's refund will be paid or will be intercepted for government debts.

"We are pleased that IRS has decided to stop aiding and abetting high cost RALs that siphon off hundreds of millions in taxpayers' hard-earned money and federal benefits meant to lift the working poor out of poverty," declared Chi Chi Wu, NCLC Staff Attorney.

RALs are one to two week loans made by banks and facilitated by commercial preparers, secured by the taxpayer's refund. In 2008, RALs skimmed $738 million from the refunds of 8.4 million American taxpayers. RALs can be expensive, with some lenders charging fees that translate into Annual Percentage Rates (APRs) of 50% to nearly 500%. They expose taxpayers to unmanageable debt if a problem with a refund results in the loan being unpaid.

Advocates at NCLC and CFA have been urging the IRS to end the debt indicator since 2005, when they published a report entitled "Corporate Welfare for the RAL Industry: The Debt Indicator, IRS Subsidy, And Tax Fraud." Their most recent criticism of the debt indicator was during the IRS Commissioner's Return Preparer Review Forum in August 2009, in which they again urged the IRS to discontinue the program.

"The federal government should not be sharing taxpayers' personal information for the profit of banks and tax preparers by operating what is essentially a free credit reporting service for them," said Jean Ann Fox, director of financial services for Consumer Federation of America. "We are glad the IRS finally stopped letting tax preparers and banks pry into taxpayers' records about what they owe the government."

Another development by the IRS is that it will explore the idea of permitting a portion of tax refunds to go directly to pay for tax preparation. This idea could help undercut the market for RALs and a related non-loan product, refund anticipation checks. Some taxpayers use RALs and RACs to avoid paying out-of-pocket for the fees for tax preparation. By splitting refunds to the tax payer and the tax preparer, one incentive to pay $1 billion for RALs and RACs could be eliminated.

In January of this year, the IRS Commissioner announced another reform backed by the consumer groups – regulation of tax preparers. In the future, the IRS will require tax preparers to be registered, tested and adhere to a code of ethics.

Finally, consumer advocates called on the IRS and banking regulators to end RALs once and for all. They called on the IRS to alter its privacy rules to prohibit tax preparers from sharing or using tax return information to sell or arrange financial products, which would stop the sale of high-cost, risky loans and deposit products.

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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.

CFA is a nonprofit association of some 280 pro-consumer groups, with a combined membership of 50 million people. CFA was founded in 1968 to advance consumers' interests through advocacy and education.