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Download the report:
http://www.nclc.org/images/pdf/pr-reports/report-ral-2012.pdf

NEW NCLC/CFA REPORT DOCUMENTS TWILIGHT OF RALS AS BIG BUSINESS

End of an Era: Final Year for Bank Tax Refund Anticipation Loans

BOSTON, Mass.─As tax season shifts in to full swing, the National Consumer Law Center (NCLC) and Consumer Federation of America (CFA) have issued their annual report on the refund anticipation loan (RAL) industry. The report documents how the FDIC's settlement with the last bank making RALs spells the end of these loans as big business. *The Party's Over For Quickie Tax Loans: But Traps Remain For Unwary Taxpayers*, is available at http://www.nclc.org/images/pdf/pr-reports/report-ral-2012.pdf

The report also looks back at RAL lending in prior years, finding that the loans drained the refunds of about 5 million American taxpayers in 2010, costing them in the neighborhood of $338 million in loan fees, plus over $48 million in other fees. In addition, another 14.6 million taxpayers spent $438 million on related financial products to receive their refunds.

"It's good riddance to RALs as big business," says Chi Chi Wu, staff attorney at the National Consumer Law Center (NCLC). "Millions of hard-working families will save money and face less risk as RALs made by banks disappear from tax time."

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 and Liberty Tax 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 refund anticipation checks (RACs) has increased to an estimated 14.6 million taxpayers in 2010, up from the 12.9 million in 2009. 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, or deposits the funds to the taxpayer's bank account, and closes the temporary RAC account.

RALs are mostly marketed to low-income taxpayers, including recipients of the Earned Income Tax Credit (EITC), the nation's largest federal anti-poverty program. According to IRS data, 92% of taxpayers who applied for a RAL in 2010 were low-income, and two-thirds (66%) were EITC recipients.

Lack of Transparency in Tax Preparation Fees

Another problem faced by taxpayers is the lack of transparency around tax preparation fees. Mystery shopper testing by consumer groups and others has found systemic problems in the ability of consumers to obtain information about how much tax preparation services will cost. The NCLC/CFA report describes numerous examples of tax preparers refusing to provide estimates for tax preparation fees or giving low-ball estimates.

The ability to deduct tax preparation fees from a RAC or RAL compounds this problem by making taxpayers less sensitive to the price of preparation, since they do not pay the fees out-of-pocket. It also enables preparers to pad the price with add-on fees.

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.

Life after RALs: Refund Anticipation Checks

Even after the end of RALs, tax preparers and banks will continue to offer refund anticipation checks (RACs). 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, for which the banks generally charge about $30 - $35. Tax preparers may also charge their own "add-on" fees, which can range from $25 to several hundred dollars. This year H&R Block offered a free RAC for the first three weeks of the 2012 tax season, if the taxpayer used the Block Emerald Card to receive the refund.

Since one of their main purposes is to defer payment of the tax preparation fee until the refund arrives, RACs may represent a high-cost loan of that fee. If considered as a finance charge, a RAC fee of $30 to borrow a typical tax preparation fee of $189 for two weeks equates to an APR of 414%.

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.

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. The president of SGS Credit Services also appears to serve as the treasurer for the Texas Consumer Lenders PAC.

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 affiliated with an Ohio businessman who founded the payday loan chain Cashland.

A few storefront payday lenders appear to be pitching variations of their payday or auto title loan products as RALs. Others are promoting tax preparation or check cashing for tax refunds, but not offering RALs.

"Consumers should avoid any loans offered along with tax preparation services by financial outlets," says Jean Ann Fox. "Beware of lenders that try to divert your hard-earned tax refund dollars to repay high-cost loans or make down-payments on bad deals."

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 authorize extremely high-cost payday lending at all.

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