

# One Step Forward, One Step Back: Progress Seen in Efforts Against High-Priced Refund Anticipation Loans, but Even More Abusive Products Introduced

## The NCLC/CFA 2007 Refund Anticipation Loan Report

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### Executive Summary

- Refund anticipation loans (RALs) are high cost, high risk short-term loans secured by the taxpayer's expected tax refund. This is the annual update from the National Consumer Law Center and Consumer Federation of America on how much RALs are costing taxpayers.
- RAL volume declined dramatically from 2004 to 2005. Consumers took out approximately 9.6 million RALs during the 2005 tax-filing season compared to 12.38 million in 2004. There could be a number of reasons for this decline, including better reporting to the IRS, more public awareness of the nature of RALs, and anti-RAL advocacy.

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The 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 community groups and organizations, who represent low-income and elderly individuals on consumer issues.

Consumer Federation of America is a non-profit association of about 300 groups, with a combined membership of over 50 million people. CFA was founded in 1968 to advance consumers' interest through advocacy and education.

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- We have seen substantial progress in the reform of the RAL industry. Both industry giant H&R Block and major RAL lender JP Morgan Chase have lowered prices for some of their RALs. H&R Block is marketing debit card-based accounts that may help its low-income customers become banked and even avoid RALs in the future.
- On the other hand, the industry has promoted a line of products this past year even worse than traditional RALs – pay stub and holiday RALs. These are RALs made prior to the tax filing season, before taxpayers receive their IRS Form W-2s and can prepare and file their returns. They present additional costs and risks to taxpayers, plus they may continue the ability of the RAL industry to drain tax refunds even after the IRS speeds refund delivery times to a few days.
- The APRs for RALs can still range in the triple digits. H&R Block claims that its RALs delivered on the Block Emerald card carry an APR of 36%, but that calculation does not include the fee for the dummy account used to repay the RAL. For other providers, APRs for some of their RALs remain in the triple digits. The effective annualized interest rate for RALs based on a 10 day loan period ranges from about 40% (for a loan of \$10,000) to over 500% (for a loan of \$300). The annualized interest rate for a loan of a typical refund size of about \$2,500 can be from 85% to 170%.
- Consumers paid an estimated \$960 million in RAL fees in 2005 to get quick cash for their refunds – essentially borrowing their own money at extremely high interest rates. This represents a decrease of 22% from 2004 to 2005, but is still a tremendous drain on the tax refunds of American taxpayers.
- In addition to RAL fees, consumers paid another estimated \$100 million in “document processing” or “application fees” in 2005. This amount dropped significantly due to the fact that H&R Block and Liberty Tax dropped the fee completely. Jackson Hewitt dropped a similar fee for company-owned stores, but did not completely eliminate it until 2007 for the 87% of its stores that are franchisees.
- Substantial reforms have occurred with respect to the practice of cross lender debt collection. The California Attorney General reached a settlement with Jackson Hewitt that requires the company to inform consumers if they owe past-due RALs and that if they apply for a RAL or RAC, the proceeds will be used to satisfy this debt. JPMorgan Chase has stated it will cease cross collection altogether, except for a remaining one year for HSBC past due RALs. H&R Block has unveiled a new "debt alert" service that informs clients about a possible past-due RAL debt and provides access to a toll-free number to HSBC for more information.
- The men and women of our nation’s armed forces are a prime target for RALs, paying an estimated \$10 million out of their refunds (including EITC and Child Tax Credit benefits) for these loans. Like payday lenders, mapping of RAL facilitators shows they cluster around military bases. The recently enacted Military Lending Act should protect Service

members from high cost loans, but banks have been advocating that they be exempted from the new law, which would permit them to continue making RALs to the military.

- This year has seen concerted efforts by a number of state and local advocacy groups to combat RALs in California, Illinois, New York City, North Carolina, Philadelphia and other locations. Some of these efforts have involved work with state officials, such as the State Treasurers from North Carolina, Connecticut and New York.
- The marketing of RALs and other ancillary products was eliminated from the Free File program, which provides free Web-based electronic filing for taxpayers who make less than \$52,000 annual adjusted gross income.

## I. Introduction

Refund anticipation loans (RALs) are high cost loans secured by and repaid directly from the proceeds of a consumer's tax refund from the Internal Revenue Service (IRS). Because RALs usually run for a duration of about 7-14 days (the difference between when the RAL is made and when it is repaid by deposit of the taxpayer's refund), fees for these loans can translate into triple digit Annual Percentage Rates (APR), although prices have dropped this year for many RALs. RALs drain hundreds of millions from the pockets of consumers and the U.S. Treasury. They target the working poor, especially those who receive the Earned Income Tax Credit (EITC), a refundable credit provided through the tax system and intended to boost low-wage workers out of poverty. The EITC is the largest federal anti-poverty program, providing nearly \$40 billion to 21.7 million families in 2005.<sup>1</sup>

This report updates the NCLC/CFA annual reports on the RAL industry and the drain caused by RALs from EITC benefits. Those interested in background information on the industry and regulation should refer to the first NCLC/CFA RAL Report published in January 2002.<sup>2</sup>

We have seen significant progress in the fight against RALs. The number of RALs declined significantly in 2004, by about 22%. The volume of RALs in 2005, the most recent year for which the IRS has data, shows RAL usage at about 9.6 million. However, RALs continue to drain over \$1 billion dollars from the pockets of American taxpayers, including EITC recipients.

The price of RALs has also declined. For this year, the nation's largest tax preparation firm, H&R Block, dropped its RAL prices by 40% for loans around an average refund of \$2,500. While still higher than we'd like to see, this represents a real decline in the price of RALs for low income taxpayers, especially when coupled with the fact that Block has completely dropped its "administrative" fee averaging \$30. Another major RAL lender, JPMorgan Chase, dropped the prices for some of its RALs as well.

Other notable progress in reforming RAL practices occurred in 2006. Block has revised its cross lender debt collection practices and will be offering electronic debit card-based bank accounts to all of its customers, which can be used to save on RAL fees or check cashing fees. Chase will be dropping cross collection entirely, and Jackson Hewitt was required to reform its practices by the California Attorney General. RAL marketing was eliminated from the IRS Free File program.

On the other hand, the RAL industry took a step for the worse with the introduction of pay stub and holiday RALs, which are made prior to the tax filing season, before taxpayers

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<sup>1</sup> Data from IRS Stakeholder Partnerships, Education & Communication (SPEC) Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.

<sup>2</sup> Chi Chi Wu, Jean Ann Fox, and Elizabeth Renuart, *Tax Preparers Peddle High Priced Tax Refund Loans: Millions Skimmed from the Working Poor and the U. S. Treasury*, National Consumer Law Center and Consumer Federation of America, January 31, 2002, [hereinafter "NCLC/CFA 2002 RAL Report"], available at [www.consumerlaw.org/action\\_agenda/refund\\_anticipation/content/RAL\\_final.pdf](http://www.consumerlaw.org/action_agenda/refund_anticipation/content/RAL_final.pdf).

receive their IRS Form W-2s and can file their returns. Pay stub RALs are made in January using the year-end pay stub information, while holiday RALs are made by tax preparers during November and December. They present additional costs and risks to taxpayers, plus may continue the ability of the RAL industry to drain tax refunds even after the IRS speeds refund delivery times to a few days.

## II. RAL Volume Drops Dramatically

RAL volume declined significantly in 2005. The IRS data indicates there was a decrease of 22% in the number of RALs from 2004 to 2005. Based on the IRS data, we estimate there were approximately 9.6 million RALs made in 2005.<sup>3</sup> In our last RAL report, we estimated approximately 12.38 million RALs were taken out in 2004.<sup>4</sup> The percentage of taxpayers who took out RALs dropped as well, to about 1 in 13 taxpayers.<sup>5</sup>

In 2005, for taxpayers who received refunds, the average amount was about \$2,500.<sup>6</sup> Based on prices charged to the customers of the nation's largest tax preparation chain for that year, these taxpayers paid about \$100 in RAL fees.<sup>7</sup> Thus, taxpayers paid somewhere in the neighborhood of \$960 million in RAL fees in 2005. This compares to an estimated \$1.24 billion in RAL loan fees in 2004.<sup>8</sup> This represents a 22% decrease.

The following chart documents the trends in RALs since the 2000 filing season:<sup>9</sup>

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<sup>3</sup> The 9.6 million figure was calculated as follows: 1) IRS statistics state that there were 10.66 million tax returns which were associated with a RAL. Data from IRS SPEC, Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.; 2) we assume that since IRS would not know whether a RAL was approved or denied, so these statistics represent the number of RALs applied for.

Published materials from the RAL industry state that about 90% of RAL applications result in an approved loan. Santa Barbara Bank & Trust, *Why You Should Choose SBBT '05*, available at [www.taxwise.com/pdf/Why%20SBBT.pdf](http://www.taxwise.com/pdf/Why%20SBBT.pdf); Household International, *Exploring the Refund Anticipation Loan (RAL): Questions and Answers*, on file with the authors. Thus, 90% of 10.66 million is 9.59 million. However, some industry members have claimed that the approval rate is lower, at 85%.

<sup>4</sup> Chi Chi Wu, Jean Ann Fox, and Patrick Woodall, *Another Year of Losses: High-Priced Refund Anticipation Loans Continue To Take a Chunk Out Of Americans' Tax Refunds*, National Consumer Law Center and Consumer Federation of America, January, 2006, at 4 [hereinafter referred to as "NCLC/CFA 2006 RAL Report."].

<sup>5</sup> There were 128.6 million returns filed in the 2005 filing season, which was for Tax Year 2004. Data from IRS SPEC, Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.

<sup>6</sup> According to IRS data, 101.7 million taxpayers received refunds totaling \$249.6 billion in 2005. That averages to \$2,454 per taxpayer who received a refund. *Id.*

<sup>7</sup> Chi Chi Wu and Jean Ann Fox, *Picking Taxpayers' Pockets, Draining Tax Relief Dollars: Refund Anticipation Loans Still Slicing Into Low-Income Americans' Hard-Earned Tax Refunds*, National Consumer Law Center and Consumer Federation of America, January 2005, at 12. [hereinafter referred to as "NCLC/CFA 2005 RAL Report."].

<sup>8</sup> NCLC/CFA 2006 RAL Report at 4.

<sup>9</sup> This chart is based on the data in the annual RAL reports issued by National Consumer Law Center and Consumer Federation of America: NCLC/CFA 2006 RAL Report at 4; NCLC/CFA 2005 RAL Report at 4; Chi Chi Wu and Jean Ann Fox, *All Drain, No Gain: Refund Anticipation Loans Continue to Sap the Hard-Earned Tax Dollars of Low-Income Americans*, January 2004, at 4 [hereinafter referred to as "NCLC/CFA 2004 RAL Report."]; Chi Chi Wu and Jean Ann Fox, *The High Cost of Quick Tax Money: Tax Preparation, 'Instant Refund' Loans, and Check Cashing Fees Target the Working Poor*, National Consumer Law Center and Consumer Federation of America, January 2003, at 1 [hereinafter referred to as "NCLC/CFA 2003 RAL Report."]; NCLC/CFA 2002 RAL Report at 4.

<b>Filing Year</b>	<b>No. of RALs</b>	<b>Increase/decrease from prior year</b>	<b>RAL loan fees</b>
2005	9.6 million	(-22)%	\$960 million
2004	12.38 million	1.89%	\$1,240,000,000
2003	12.15 million	(-4)%	\$1,090,000,000
2002	12.7 million	5%	\$1,140,000,000
2001	12.1 million	12%	\$907,000,000
2000	10.8 million	--	\$810,000,000

The \$960 million for 2005 does not include the added fees paid for loan products that provide a RAL on the same day that the taxpayer's return is prepared.<sup>10</sup> Lenders charge an additional \$25 to \$55 for same-day RALs, a fee which the consumer pays on top of regular RAL fees.<sup>11</sup> We know that H&R Block made 1.5 million "Instant Money" RALs in 2004.<sup>12</sup> Assuming a similar number in 2005, this adds at least another \$37.5 million to the RAL drain.<sup>13</sup> We do not have data on the number of same-day RALs made by the rest of the industry.

In addition to the RAL loan fee, at one time, all of the major tax preparation firms had been charging their own separate fees for RALs, sometimes called a "document processing" or "application" fee. However, H&R Block had dropped this fee entirely by 2005 as part of an agreement with ACORN.<sup>14</sup> A Jackson Hewitt representative testified in a 2005 Senate hearing that the chain agreed to drop this fee entirely in its company-owned offices and to encourage its franchisees to do the same.<sup>15</sup> However, over 4,800 of the approximately 5,500 Jackson Hewitt offices (or 87%) are franchisees,<sup>16</sup> and Jackson Hewitt apparently only committed to eliminating the fee for all its offices for the 2007 filing season.<sup>17</sup> Liberty Tax agreed to drop its application fee as a result of advocacy by ACORN.<sup>18</sup>

<sup>10</sup> This \$960 million also does not include fees for pay stub or holiday RALs, discussed in Section VII below.

<sup>11</sup> H&R Block, *Sample Refund Anticipation Bank Loan*, January 2006, on file with the authors; Santa Barbara Bank & Trust, *2006 Program Newsletter for Tax Professionals*, available at the Taxwise website at [www.taxwise.com/pdf/2006%20SBBT%20Newsletter.pdf](http://www.taxwise.com/pdf/2006%20SBBT%20Newsletter.pdf).

<sup>12</sup> Peter Tufano and Daniel Schneider, *H&R Block and "Everyday Financial Services,"* Harvard Business School, October 2004, at 7.

<sup>13</sup> Note that Block customers pay an additional \$25 for an Instant RAL. H&R Block, *Sample RAL and Instant RAL*, January 2007, on file with the authors. This is significantly less than the same-day RAL surcharge for other tax preparers; thus, the drain created by these products may even be greater if we had data on industry-wide sale.

<sup>14</sup> ACORN and H&R Block Press Release, *H&R Block and ACORN Partner To Help Working Families Claim And Keep More Of What They've Earned This Tax Season*, January 14, 2005.

<sup>15</sup> Testimony of Gary P. Weinstein, Vice President, Legal and Government Affairs, Jackson Hewitt Tax Service, Before the Permanent Subcommittee on Investigations, April 15, 2005.

<sup>16</sup> Jackson Hewitt Tax Service Inc., *2005 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 3 [hereinafter "Jackson Hewitt 2005 Form 10-K".]

<sup>17</sup> ACORN Financial Justice Center, *Missing Millions: Expanding Access to the Earned Income Tax Credit While Reducing Reliance on Refund Anticipation Loans*, ACORN, January 2007, at 9.

<sup>18</sup> *Id.*

RAL lender Santa Barbara Bank & Trust has stated that its tax preparers may charge a document processing fee up to \$40.<sup>19</sup> Given that Jackson Hewitt did not drop its fee until April 2005 and mostly for company-owned stores, we will assume some portion of Hewitt offices continue to charge the application fee in 2005.<sup>20</sup> In addition, HSBC alone has reported partnerships with several thousand independent preparers.<sup>21</sup> Independent preparers have about 70% of the paid preparer market.<sup>22</sup> We assume that the Jackson Hewitt franchisees and independent preparers who did not drop the document processing fee comprised only 25% of the market charged the fee, which would equate to 2.5 million consumers.<sup>23</sup> Using SBBT's figure of \$40, these additional fees added about \$100 million to the amount paid for RALs in 2005.

### III. Reasons for Decline in RALs

At this point, we do not have solid information as to the reasons for the decline in RALs from 2004 to 2005. We can cite to a number of possible reasons, any one of which alone or in combination with other reasons may explain the decline in RALs.

One potential reason is better reporting to the IRS in the number of RALs. Industry sources have previously claimed that the IRS data on RALs includes some non-loan products,<sup>24</sup> such as refund anticipation checks (RACs).<sup>25</sup> However, the IRS had never stated that its data included non-loan RACs, and we had only the IRS data on which to rely. The National Taxpayer Advocate's 2005 Annual Report to Congress implied there was a greater effort to include only RALs starting in 2005, and this could explain the decline.<sup>26</sup>

For 2006, the IRS has instituted a change in the RAL indicator by explicitly requiring tax preparers to indicate whether an electronically filed return is associated with a RAL versus a

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<sup>19</sup> Plaintiff's Local Rule 56(a)(1) Separate Statement of Undisputed Facts at ¶8, n. 1, *Pacific Capital Bank, N.A. v. Conn.*, No. 3:06-CV-28 (D. Conn. Aug. 10, 2006).

<sup>20</sup> Testing by advocates in Philadelphia confirmed that some Jackson Hewitt offices did charge the document processing fee in 2006. Letter to Jackson Hewitt Chairman Michael Lister from Community Legal Services, April 4, 2006, at 2.

<sup>21</sup> HSBC has reported that H&R Block offices make up only 9,200 of the 17,300 (or 53%) outlets with which HSBC does RAL business. Household International, *2003 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 7 [hereinafter "Household 2003 Form 10-K"]. While some of the remaining 8,100 offices may be Jackson Hewitt franchisees, it appears that there are still several thousand independent preparers with which HSBC has a relationship.

<sup>22</sup> NCLC/CFA 2005 RAL Report at 15; Jackson Hewitt Tax Service, *Investor Presentation – December 2006 Update*, November 22, 2006, at 8.

<sup>23</sup> In 2005, Block had 4 million RALs (see Section VII below) or about a 42% share of the market. We conservatively assume that less than half of the remaining market is charged a document processing fee.

<sup>24</sup> See, e.g., Email from Santa Barbara Bank & Trust to authors, on file with authors.

<sup>25</sup> Refund anticipation checks are the non-loan bank product that many RAL lenders and tax preparers offer in addition to RALs. With refund anticipation checks, the bank opens a temporary or "dummy" bank account into which the IRS direct deposits the refund check. After the direct deposit of the consumer's refund, the bank issues the consumer a paper check and closes the dummy account. The consumer then picks up the check from the tax preparer's office.

<sup>26</sup> National Taxpayer Advocate, *FY 2005 Annual Report to Congress*, December 31, 2005, at 164 [hereinafter "National Taxpayer Advocate 2005 Report"].

RAC.<sup>27</sup> This should ensure accurate results without having RACs included in the RAL figure. Indeed, with this change in reporting, preliminary information indicates the number of RAL applications reported for 2006 has declined about 5-6%.<sup>28</sup> This change in IRS reporting will also allow us to calculate the number of RACs and dollars paid for that product. Preliminary information from the IRS shows that 9.7 million taxpayers applied for RACs in 2006, costing them at least \$240 million.<sup>29</sup>

The decline in RALs could also indicate a real drop in RALs for 2005 due to the cumulative effect of improved disclosures and several years of anti-RAL education efforts. The past several years have seen modest reforms in RAL disclosures. For example, Block saw an 8% decline in RALs when it improved its disclosures.<sup>30</sup> Other tax preparation chains and RAL lenders have revised their disclosures, plus a number of states passed laws requiring better RAL disclosures.<sup>31</sup>

Public awareness of the problems with RALs could also account for some of the decline. During the last several years, there have been a substantial number of media articles and broadcast pieces advising consumers against RALs, in part a result of advocacy by consumer groups, such as those discussed in Section XIII. These articles have been appearing in January (when it could actually impact RAL volume) as opposed to April (when late filers who usually don't seek RALs send in their returns). Note that when Block stopped advertising RALs in San Francisco, that city saw a 16% decline in the number of RALs, indicating the media environment around RALs can affect volume.<sup>32</sup> Another contributor to public awareness has been greater communication and better disclosure that taxpayers can receive refunds in 8-15 days with electronic filing and direct deposit.

Free tax preparation programs may have contributed to the decline in RALs. Many of these programs do more than prepare taxes; they engage in asset building, opening bank accounts, financial education, anti-RAL education, advocacy for the EITC, and other programs. They provide both a free alternative to commercial preparation, as well as outreach to encourage EITC participation and to avoid RALs. The National Community Tax Coalition operates as an umbrella for this community, and a listing of NCTC members can be found at [www.tax-coalition.org](http://www.tax-coalition.org).

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<sup>27</sup> IRS, Publication 1346, Electronic Return File Specifications For Individual Income Tax Returns Tax Year 2005, August 30, 2005, at xi.

<sup>28</sup> An IRS official indicated that there were 10 million returns associated with a RAL application in 2006, as opposed to the 10.66 million in 2005 as indicated by the IRS SPEC database.

<sup>29</sup> IRS, Report to Congress, November 2006, at 21. The cost of a RAC ranged from \$25 to \$30 in 2006. See 2006 NCLC/CFA Report at 6.

<sup>30</sup> H&R Block Inc., *2004 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 17. [hereinafter "H&R Block 2004 Form 10-K"].

<sup>31</sup> See 2005 NCLC/CFA RAL Report at 10; Section XII below.

<sup>32</sup> Tim Flacke and Tiana Werthein, *Delivering a Local EITC: Lessons from the San Francisco Working Families Credit*, Brookings Institution and SF Works, May 2006, at 12.



#### IV. Price Drop for RALs in 2007

On September 7, 2006, H&R Block announced a major price decrease for RALs in the range of its average loan, around \$2,800, from \$100 to \$60. This price decrease applies if the RAL is deposited into the Block Emerald Card.<sup>33</sup> Block asserts that this RAL, and all RALs deposited on the Emerald Card, now carry an APR of only 36%, which is a traditional maximum small loan rate cap for state usury laws. However, Block's calculation of their APRs does not include the \$29.95 charged for the "Refund Account Fee." This is the fee supposedly for the "dummy" bank account used to receive the consumer's tax refund from IRS to repay the RAL. Most tax preparers and RAL lenders do not include this fee in the APR, claiming that it is comparable to the charge for the non-loan RAC product. We have challenged this unbundling in the past, for reasons explained in past RAL reports.<sup>34</sup>

If the dummy account fee is included, the APRs increase, quite dramatically for the loans in the lowest tier (\$300 to less than \$1,000), and can still be in the triple digits. Nonetheless, Block's prices do represent a substantial price drop for the middle tier of its loans (\$1,000 to \$4,000).

#### H&R Block/HSBC 2007 Sample RAL fees<sup>35</sup>

Amount of Loan	Loan Fee w/ Emerald Card	Loan Fee w/ Paper Check
\$300	\$33.17	\$36.15
\$500	\$35.31	\$40.28
\$750	\$37.99	\$45.44
\$1,000	\$40.68	\$50.61
\$1,500	\$46.04	\$60.94
\$2,000	\$51.41	\$71.27
\$3,000	\$62.14	\$91.93
\$4,000	\$72.87	\$112.59
\$5,000	\$83.60	\$133.25
\$9,999	\$137.23	\$236.52

We do not have prices for Jackson Hewitt; however, we do have prices charged by Santa Barbara Bank & Trust for independent preparers.<sup>36</sup> SBBT's prices are higher, and appear to have been increased \$10 to \$15 from its 2006 prices for certain loan ranges (\$300 to \$500 and \$3,501 to \$9,999).<sup>37</sup>

<sup>33</sup> Press Release, *H&R Block Announces Plan to Open 1 Million Bank Accounts for Free and Significantly Cut the Cost of Refund Lending*, September 7, 2006.

<sup>34</sup> For an analysis of why the fee for the dummy bank account should be included in the APR, see NCLC/CFA 2004 RAL Report at 5.

<sup>35</sup> H&R Block, *Sample Refund Anticipation Bank Loan*, January 2007, on file with the authors.

<sup>36</sup> *2007 Santa Barbara Bank & Trust Fact Sheet*, available at <http://www.taxview.com/factsheets/2006SBBT.pdf>.

<sup>37</sup> See NCLC/CFA 2006 RAL Report at 17 for last year's SBBT pricing.

### **SBBT 2007 RAL Fee Schedule**

<b>Amount of Loan</b>	<b>Loan Fee</b>
\$300- \$1,000	\$43.95
\$1,001-1,500	\$68.95
\$1,501-\$2,000	\$83.95
\$2,001-\$3,500	\$110.95
\$3,501-\$9,999	\$120.95

JPMorgan Chase also has dropped RAL fees for some of its RALs, especially in the lower range of \$500 to \$1,000.<sup>38</sup> Chase's loan fees are as follows:<sup>39</sup>

### **JPMorgan Chase 2007 RAL Fee Schedule**

<b>Amount of Loan</b>	<b>Loan Fee</b>
\$300-\$1,000	\$33
\$1,000- \$1,500	\$69
\$1,501-\$2,000	\$79
\$2,001-\$3,500	\$104
\$3,501-\$10,000	\$114

Thus, for RALs in 2007, a consumer can expect to pay from \$57 (Block) to \$111 (SBBT) in order to get a RAL for a typical refund of about \$2,500. The effective APR for this RAL would be 85% (Block) to 150% (Chase) to 170% (SBBT).

Thus, we are finally seeing some competition in RAL pricing. For years, the major RAL lenders and their tax preparation partners appeared to offer prices that were within a few dollars of each other. More importantly, industry players did not advertise or promote lower prices to consumers. We have seen this year the first sign of competitive pricing in the RAL marketplace.

Still, RALs continue to represent a huge drain on the tax refunds of nearly 10 million consumers. Moreover, the fee for the RAL comes on top of the fee for tax preparation, which typically could be around \$150.<sup>40</sup> Altogether, the consumer might pay about \$207 to \$260. If the consumer chooses a tax preparer that charges a "document processing" or "application" fee of \$40 per loan, the total would rise to as much as \$300.<sup>41</sup> A low-income taxpayer could save this entire amount and still receive a quick refund using direct deposit by choosing a free tax preparation program that offers e-filing.

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<sup>38</sup> See *id.* at 18 for last year's Chase pricing.

<sup>39</sup> JPMorgan Chase, Refund Anticipation Loan and/or Bonu\$ Deposit Account with Cahier's Check 2007, on file with authors.

<sup>40</sup> According to industry leader H & R Block, its average tax preparation fee is about \$150. H&R Block Inc., 2005 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, at 22.

[hereinafter "H&R Block 2005 Form 10-K"]. Higher fees have been reported anecdotally. For example, testing done by advocates in Philadelphia revealed tax preparation fees of \$345 by Jackson Hewitt and \$243 by H&R Block. Letter to H&R Block Chairman Mark Ernst from Community Legal Services, April 4, 2006; Letter to Jackson Hewitt Chairman Michael Lister from Community Legal Services, April 4, 2006.

<sup>41</sup> The U.S. Government Accountability Office reported even higher amounts charged for RALs, between \$470 and \$570. U.S. Government Accountability Office, *Paid Tax Preparers: In a Limited Study, Chain Preparers Made Serious Errors*, GAO-06-563T, April 4, 2006, at 24, available at <http://www.gao.gov/new.items/d06563t.pdf>.

For the 2007 filing season, the APRs on RALs vary widely given the divergence in pricing between the industry players. They can be anywhere from about 40% (for a loan of \$10,000) to over 500% (for a loan of \$300).<sup>42</sup> We also continue to report a version of the APR that includes application or document processing fees, if they are charged, because those fees when charged also represent a cost of the credit for a RAL.<sup>43</sup> For loans with document processing or application fees, the fees can translate into APRs of about 57% (\$10,000 loan) to over 1,100% (\$300 loan).

## V. Impact on Low-Income Taxpayers and EITC recipients

RALs are mostly marketed to low-income taxpayers. According to IRS data, 83% of RAL applicants in 2005 had adjusted gross incomes of \$35,000 or less.<sup>44</sup> This is consistent with statistics that 57% of H & R Block's customers make less than \$30,000 annually.<sup>45</sup> Jackson Hewitt similarly reports in its SEC filings that 73% of its customers make less than \$30,000 adjusted gross income,<sup>46</sup> and HBSC states that the majority of their RAL customers have an average household income of \$17,800.<sup>47</sup> A 2005 survey by CFA found that the majority of RAL borrowers (58.7%) earned below \$40,000.<sup>48</sup>

Despite the decline in volume, RALs continue to drain hundreds of millions from the Earned Income Tax Credit. IRS data shows that in 2005 over 60% of RAL consumers were EITC recipients, or 5.9 million families.<sup>49</sup> Yet EITC recipients made up only 17 % of individual taxpayers in 2005.<sup>50</sup> Thus, EITC recipients are vastly overrepresented among the ranks of RAL consumers. In addition, IRS data shows that 30% of EITC recipients applied for a RAL in 2005.<sup>51</sup>

Based on this IRS data, we estimate that about \$590 million was drained out of the EITC program in 2005 by RAL loan fees.<sup>52</sup> Administrative/application fees added another \$59 million to the drain.<sup>53</sup>

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<sup>42</sup> These APRs are based upon a 10 day loan period. The estimated time provided by the federal government to receive a refund with e-filing and direct deposit is 8 to 15 days. IRS, *IRS e-file 2007 Refund Cycle Chart*, Publication 2043, October 2006. The median time would be 11.5 days, and the loan itself takes one or two days to process.

<sup>43</sup> The U.S. Government Accountability Office reported instances of RAL APRs that were 380% and 470%. U.S. Government Accountability Office, *Paid Tax Preparers: In a Limited Study, Chain Preparers Made Serious Errors*, GAO-06-563T, April 4, 2006, at 24, available at <http://www.gao.gov/new.items/d06563t.pdf>.

<sup>44</sup> Data from IRS SPEC, Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.

<sup>45</sup> David Rose, Daniel Schneider, and Peter Tufano, *H&R Block's Refund Anticipation Loans: Perilous Profits and the Bottom of the Pyramid*, Harvard Business School, March 1, 2006, at 1.

<sup>46</sup> Jackson Hewitt, *Final Prospectus*, June 22, 2004, at 46.

<sup>47</sup> Household 2003 Form 10-K at 7.

<sup>48</sup> NCLC/CFA 2006 RAL Report at 12.

<sup>49</sup> IRS data reports that 6.6 million EITC returns were associated with a RAL in 2005. Data from IRS SPEC, Tax Year 2004 Return Information (Returns Filed in 2005), November 2006. Using the 90% approval rate, see note 3 *supra*, the number of approved RALs is 5.9 million.

<sup>50</sup> There were 21.7 million EITC returns in 2005 and 128 million individual tax returns in 2005. Data from IRS SPEC, Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.

<sup>51</sup> Data from IRS SPEC, Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.

<sup>52</sup> At a fee of \$100 for a RAL for the average refund times 5.9 million.

Non-loan fees also drain significantly from EITC benefits. The EITC is the nation’s largest anti-poverty program. One criticism has been that no other anti-poverty program requires its beneficiaries to pay for the cost of accessing the benefit, which include both the drain created by RALs as well as tax preparation fees. Including tax preparation provides a fuller picture of how EITC benefits are chipped away. EITC recipients who got RALs paid an additional \$885 million in tax preparation fees. In addition, some percentage of these recipients paid additional check cashing fees.

<b>Type of Fee</b>	<b>Cost to Taxpayer</b>	<b>Drain on EITC Program</b>
RAL loan fee (inc. dummy account fee)	\$100	\$590 million
Application/Admin. Fee (for 25%)	\$40	\$59 million
<b>Total</b>	<b>\$140</b>	<b>\$649 million</b>
Tax preparation fee	\$150	\$885 million
<b>Total with tax preparation</b>	<b>\$290</b>	<b>\$1.5 billion</b>

Each of these fees undermines the effectiveness of the EITC in supporting low-wage workers. These fees transfer billions in wealth, paid out of the U.S. Treasury, from poor families to multi-million dollar corporations.

## **VI. Overview of Key Industry Players**

This section provides basic information on the RAL activity of key industry players, an overview that we provide annually in our RAL reports. We discuss certain other topics affecting these players, such as law enforcement actions, reform measures by certain companies, and other events, in other parts of this report.

### H&R Block

H&R Block is the nation’s largest tax preparation chain, accounting for 15.5% of all individual tax returns in 2005.<sup>54</sup> In 2005, Block’s RAL business stayed essentially flat. Block made 4.2 million RALs, compared to 4.27 million in 2004.<sup>55</sup> The company did experience a significant decline in RALs, but interestingly this occurred in 2004 not 2005.<sup>56</sup> In 2006, the number of Block-facilitated RALs declined again to 4 million.<sup>57</sup>

Block processed 19.1 million tax returns in 2005;<sup>58</sup> thus, 22% of its customers received RALs in 2005. Block earns fees from RALs through its arrangement to have Block Financial Corporation buy a 49.9% interest in RALs arranged by the tax preparation arm.

<sup>53</sup> Weighted to 25%, *see* Section II *supra*.

<sup>54</sup> H&R Block 2005 Form 10-K at 3.

<sup>55</sup> H&R Block 2005 Form 10-K at 22; H&R Block 2004 Form 10-K at 17.

<sup>56</sup> *See* NCLC/CFA 2006 Report at 13.

<sup>57</sup> H&R Block Inc., *2006 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 25. [hereinafter “H&R Block 2006 Form 10-K”].

<sup>58</sup> H&R Block 2005 Form 10-K at 17.

In 2005, Block earned \$182.2 million in revenues from RALs, representing almost 8% of the company's revenues.<sup>59</sup> In 2006, Block's RAL profits dipped to \$178 million, or 7.3% of revenue.<sup>60</sup>

Block has instituted a number of reforms, such as reduced RAL pricing, low-cost bank accounts, and cross collection reforms, which are discussed in other sections of this report. In 2006, Block obtained the bank charter it had long sought from the Office of Thrift Supervision (OTS).<sup>61</sup>

## HSBC

HSBC reported that in 2005, it had over 9 million refund product customers.<sup>62</sup> It is unclear whether these accounts were all RALs, or whether some RACs were included in the mix. HSBC's RAL/RAC income was \$277 million in 2005, represented a 23% increase from its income of \$217 million in 2004.<sup>63</sup>

HSBC's price structure for RALs in 2007 for Block RALs is set forth in Section IV above. For non-Block RALs, HSBC charges \$29.95 (for its dummy account fee) and 2.75% of the loan amount.<sup>64</sup> Thus, some sample HSBC RAL fees would be:

### **HSBC Sample RAL Fees - non-Block RALs**

<b>Amount of Loan</b>	<b>Loan Fee</b>
\$300	\$38.20
\$500	\$43.70
\$1,000	\$57.45
\$1,500	\$71.20
\$2,000	\$84.95
\$3,000	\$112.45
\$4,000 and above	\$126.95

HSBC appears to have decreased RAL fees from last year for non-Block RALs as well, for certain loan amounts (\$1,001 to \$3,000).<sup>65</sup>

<sup>59</sup> H&R Block 2005 Form 10-K at 22.

<sup>60</sup> H&R Block 2006 Form 10-K at 25.

<sup>61</sup> Press Release, *H&R Block Receives Green Light To Offer Banking Products And Services*, H&R Block, March 15, 2006.

<sup>62</sup> HSBC Finance Corp., *2005 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 11 [hereinafter "HSBC 2005 Form 10-K"].

<sup>63</sup> *Id.* at 48.

<sup>64</sup> From HSBC's website at

[https://www.hsbctaxpayerfinancialservices.com/ero/products/refund\\_anticipation\\_loan.html](https://www.hsbctaxpayerfinancialservices.com/ero/products/refund_anticipation_loan.html).

<sup>65</sup> For HSBC's prices for non-Block RALs, see NCLC/CFA 2006 RAL Report at 15.

## Jackson Hewitt

Jackson Hewitt is the second largest tax preparation chain in the country, preparing 3.3 million returns in 2005, or about 2% of all individual tax returns.<sup>66</sup> Its main bank partner for RALs and other tax financial products is Santa Barbara Bank and Trust (SBBT). Jackson Hewitt also has a partnership with HSBC, which makes about 20% of the RALs and refund anticipation checks brokered by Jackson Hewitt.<sup>67</sup>

In 2005, Jackson Hewitt sold 2.4 million tax refund products, including 1.2 million RALs, up 7% from the year before.<sup>68</sup> In total, about 3.1 million of Jackson Hewitt customers, or 94%, were sold a financial product.<sup>69</sup>

In 2006, Jackson Hewitt processed 3.7 million tax returns.<sup>70</sup> About 3.4 million of these taxpayers, or 92%, were sold a financial product.<sup>71</sup> Given its 10% growth in financial products from 2005 to 2006,<sup>72</sup> we assume Jackson Hewitt brokered about 1.3 to 1.4 million RALs in 2006.

Jackson Hewitt continues to derive a startling percentage of its profits from financial products. About 28% of the company's revenues are derived from RALs alone,<sup>73</sup> a much higher percentage than Block. It earned \$80 million in financial product fees in 2006, about 40% of its revenues.<sup>74</sup>

Jackson Hewitt's RAL revenues have increased dramatically over the past few years. In 2001, the company earned only about \$20 million in financial product fees.<sup>75</sup> In 2006, Jackson Hewitt negotiated a new agreement with SBBT and HSBC over RAL fees.<sup>76</sup> Previously, Jackson Hewitt had received a fee per RAL, plus a percentage of profits.<sup>77</sup> Under the new agreement, Jackson Hewitt receives a lump sum every year from SBBT and HSBC as "compensation for being granted access to our customers and for receiving technology services, and our provision of related services."<sup>78</sup> In addition, Hewitt receives a "variable payment tied to growth in the programs."<sup>79</sup>

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<sup>66</sup> Jackson Hewitt 2005 Form 10-K at 3.

<sup>67</sup> Jackson Hewitt, *Final Prospectus*, June 22, 2004, at 30.

<sup>68</sup> Jackson Hewitt 2005 Form 10-K at 24.

<sup>69</sup> Jackson Hewitt 2005 Form 10-K at 4.

<sup>70</sup> Jackson Hewitt Tax Service Inc., *2006 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 2 [hereinafter "Jackson Hewitt 2006 Form 10-K"].

<sup>71</sup> *Id.* at 25. This includes RALs, RACs and Hewitt's "Gold Guarantee."

<sup>72</sup> *Id.* at 30.

<sup>73</sup> Jackson Hewitt 2005 Form 10-K at 15.

<sup>74</sup> Jackson Hewitt 2006 Form 10-K at 29.

<sup>75</sup> Jackson Hewitt, *Final Prospectus*, June 22, 2004, at 29-30.

<sup>76</sup> Jackson Hewitt 2006 Form 10-K at 22.

<sup>77</sup> NCLC/CFA 2006 RAL Report at 16.

<sup>78</sup> Jackson Hewitt 2006 Form 10-K at 22.

<sup>79</sup> *Id.*

## Santa Barbara Bank & Trust/Pacific Capital Bancorp

Jackson Hewitt's RAL partner, Santa Barbara Bank & Trust (SBBT), a subsidiary of Pacific Capital Bancorp, originated 5.6 million RALs and refund anticipation checks in 2005.<sup>80</sup> The product mix for that year was 70% refund anticipation checks and 30% RALs.<sup>81</sup> This means SBBT made about 1.68 million RALs in 2005.

SBBT earned \$64.7 million in RAL fees in 2005 and \$25 million in refund anticipation check fees.<sup>82</sup> About one-third of the bank's pre-tax earnings come from RALs and refund anticipation checks.<sup>83</sup>

SBBT reported that its 2006 RAL and refund anticipation check volume increased to approximately 6.7 million.<sup>84</sup> The product mix for that year was again 70% refund anticipation checks and 30% RALs.<sup>85</sup> This means that SBBT made about 2 million RALs in 2006.

## Other industry players

In addition to HSBC/ and Santa Barbara Bank & Trust, there are a handful of other banks that make RALs. The largest of these banks is JPMorgan Chase. Others include Republic Bank & Trust in Kentucky and River City Bank. The pool of RAL lenders shrank with the departure of First Bank of Delaware when that bank unexpectedly declined to offer pay stub loans for Liberty Tax Service, causing Liberty to switch its RAL business to HSBC and SBBT.<sup>86</sup>

Liberty Tax is the third significant commercial tax preparation chain in the country, with over 1,700 locations.<sup>87</sup> It processed about 1 million returns in 2005.<sup>88</sup> Its president claimed that only 16% of Liberty customers received a RAL, or about 160,000.<sup>89</sup>

## **VII. Pay Stub and Holiday RALs**

While we saw some reform in the RAL industry in 2006, we also noted the worst development in the RAL industry in several years – pay stub and holiday RALs. These are loans

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<sup>80</sup> Pacific Capital Bancorp, *Form 10-Q: Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarterly Period Ended June 30, 2005*, at 57.

<sup>81</sup> *Id.*

<sup>82</sup> Pacific Capital Bancorp, *2005 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 64. [hereinafter "PCB 2004 Form 10-K"]

<sup>83</sup> *Id.* at 11.

<sup>84</sup> Pacific Capital Bancorp, *Form 10-Q: Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarterly Period Ended June 30, 2006*, at 50.

<sup>85</sup> *Id.*

<sup>86</sup> Benjamin Lowe, *Bank Says It Will End Tax-Refund Lending*, Philadelphia Inquirer, July 27, 2006 at C1.

<sup>87</sup> Novelda Sommers, *Head of Liberty Tax Services Takes On Competition One Block at a Time*, Newport News Daily Press, March 28, 2005.

<sup>88</sup> Press Release, *Liberty Tax Service Continues Pace as Fastest Growing Tax Service Now and Ever*, Liberty Tax Service, July 23, 2005.

<sup>89</sup> Mary Wisniewski, *Bill Designed to Kill Off Tax Refund Loans*, Chicago Sun-Times, April 6, 2005.

made prior to the tax filing season, before taxpayers receive their IRS Form W-2s and can file their returns. Pay stub RALs are made in January using the year-end pay stub information, while holiday RALs are made during November and December. Both types of loans are expected to be repaid from the consumer's anticipated tax refund.

Pay stub and holiday RALs drain additional money from the tax refunds of low-income taxpayers with fees that can be as high as \$102, translating into triple digit APRs (although the pay stub RALs made by Block are supposed to be capped at 36% APR). In addition, Jackson Hewitt charges a \$50 "deposit" for tax preparation services when making the loan. Pay stub RALs also pose additional risks to consumers, because they are based on estimated tax returns before the taxpayer receives final tax information from a W-2. In addition, Jackson Hewitt appeared to be forcing pay stub RAL borrowers to return to the same office to have their taxes prepared, preventing these taxpayers from going to competitors or seeking free volunteer assistance.

The most significant policy issue posed by pay stub and holiday RALs is the fact that they will enable the RAL industry to further drain tax refunds and EITC benefits despite IRS efforts to speed refunds. The RAL industry appears to be developing in the direction of earlier and faster loans at more expense and more risk to cash-strapped families.

NCLC and CFA issued a report in November 2006 on these products, available at [www.consumerlaw.org/action\\_agenda/refund\\_anticipation/content/PaystubRALsReport.pdf](http://www.consumerlaw.org/action_agenda/refund_anticipation/content/PaystubRALsReport.pdf). Subsequently, NCLC, CFA and a number of consumer groups sent a letter calling upon the Comptroller of Currency to require national banks to cease making pay stub and holiday RALs.<sup>90</sup> There has been no reply from the Comptroller.

### **VIII. Cross Lender Debt Collection Reforms**

This past year, we have seen substantial reforms with respect to the practice of cross lender debt collection. The California Attorney General reached a settlement with Jackson Hewitt that requires the company to reform its cross collection practices in California. Jackson Hewitt must inform consumers if they owe past-due RALs and that if they apply for a RAL or RAC, the proceeds will be used to satisfy this debt.<sup>91</sup> Additional discussion of the California Attorney General's settlement can be found in Section XV.

JPMorgan Chase has stated it will cease cross collection altogether by 2008.<sup>92</sup> For 2007, Chase will only use cross collection for one other RAL lender pursuant to an existing contract, and will not authorize other RAL lenders to cross collect debt owed to Chase, which remains in effect through 2007.

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<sup>90</sup> Letter from Consumer Groups to Comptroller of Currency John Dugan, December 18, 2006, available at [http://www.consumerlaw.org/action\\_agenda/refund\\_anticipation/content/RALsPaystubOCCLetter.pdf](http://www.consumerlaw.org/action_agenda/refund_anticipation/content/RALsPaystubOCCLetter.pdf).

<sup>91</sup> Judgment, *People of the State of California v. Jackson Hewitt*, Case No. 070304558 (Cal. Sup. Ct. Alameda Cty Jan. 3, 2007), available at [http://ag.ca.gov/cms\\_pdfs/press/2007-01-03\\_Jackson\\_Hewitt\\_Settlement\\_Judgment.pdf](http://ag.ca.gov/cms_pdfs/press/2007-01-03_Jackson_Hewitt_Settlement_Judgment.pdf).

<sup>92</sup> Email from JP Morgan Chase to Consumer Federation of America, National Consumer Law Center, Woodstock Institute and Center for Economic Progress, November 6, 2006, on file with authors.



H&R Block has unveiled a new "debt alert" service that informs clients about a possible past-due RAL debt. Block will then provide access to a toll-free number to HSBC for more information on any debt owed.<sup>93</sup>

Hopefully, these reforms will result in fewer taxpayers losing their current tax refunds to what has been a particularly abusive practice in the RAL industry. These reforms were probably necessary to comply with various consumer protection laws, including the federal Fair Debt Collection Practices Act.

## **IX. RALs Dropped from Free File**

Another notable victory in the battle against RALs occurred in 2006 when the IRS announced that RALs would no longer be offered by the Free File program.<sup>94</sup> For years, we had urged the IRS to prohibit the commercial tax preparation websites participating in Free File from marketing RALs through the program.<sup>95</sup> We had argued that since taxpayers reach Free File preparers by going through [www.irs.gov](http://www.irs.gov), RAL marketing to Free File taxpayers was an implicit government endorsement of RALs. In addition, in April 2006, then Senate Finance Committee Chair Charles Grassley sent a letter to the IRS critical of the Free File program, including the marketing of a whole array of ancillary products and services to taxpayers.<sup>96</sup> Senator Grassley's letter noted one example of a Free File site that contained a link for taxpayers to purchase a tax preparation franchise for \$15,500.<sup>97</sup>

The industry's prior insistence on the ability to promote RALs in Free File was puzzling given that only 0.5% of Free File taxpayers got RALs.<sup>98</sup> In total, only 6% of Free File taxpayers got ancillary products, although half of these taxpayers said their purchase was not intended.<sup>99</sup>

A better alternative to Free File would be for Congress to enable and fund the IRS to allow taxpayers to electronically file their tax returns directly with the IRS without the need for a third party intermediary. In April 2006, Senators Akaka and Bingaman introduced the "Free Internet Filing Act" which would require the Internal Revenue Service to provide for free direct electronic filing through the IRS website.<sup>100</sup> NCLC, CFA, and other consumer groups supported this bill and opposed a contrary bill that would prohibit the IRS from providing free electronic filing services except through the Free File program and certain limited venues.<sup>101</sup>

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<sup>93</sup> Press Release, *H&R Block, HSBC Announce Refund Lending Enhancements*, October 31, 2006.

<sup>94</sup> Press Release, *RALs Removed on Free File, 93 Million Eligible for Program*, Internal Revenue Service, December 5, 2006.

<sup>95</sup> See 2006 NCLC/CFA Report at 21; 2004 NCLC/CFA Report at 16; 2003 NCLC/CFA Report at 14-15.

<sup>96</sup> *Grassley Expresses Concern Over Hidden Expenses in Free File Program*, Tax Notes, April 14, 2006.

<sup>97</sup> *Id.* Congressman Charles Rangel, Chair of the House Ways and Means Committee, applauded the IRS for dropping RALs from Free File. Press Release, *Rangel Applauds IRS Commissioner for Eliminating Refund Anticipation Loans from the Free File Program*, December 5, 2006.

<sup>98</sup> Press Release, *RALs Removed on Free File, 93 Million Eligible for Program*, Internal Revenue Service, December 5, 2006.

<sup>99</sup> *Id.*

<sup>100</sup> S. 2550.

<sup>101</sup> Press Release, *Consumer Groups Support Free Direct Electronic Filing with IRS, Express Concern About Alternate Proposal To Prohibit Free Filing*, April 21, 2006, available at [http://www.consumerlaw.org/action\\_agenda/refund\\_anticipation/content/StatementFreeInternetFiling.pdf](http://www.consumerlaw.org/action_agenda/refund_anticipation/content/StatementFreeInternetFiling.pdf).

## X. More Bank Account Options

In 2007, taxpayers will have several new options to receive their refunds. The IRS is allowing taxpayers to electronically deposit their tax refunds in up to three accounts with Form 8888. Refunds can be split by depositing into both checking and savings accounts.

Block is now offering the Emerald Card, a debit card-based account, and has announced ambitious plans to enroll 1 million of its clients into these accounts.<sup>102</sup> Block has the potential to reach a significant portion of the unbanked consumers in this country, since 3 million of its clients are unbanked.<sup>103</sup> The Emerald cards do not have an enrollment fee, nor do they carry a monthly fee for balances over \$100 or with direct deposit. There is no fee for debit card transactions.<sup>104</sup> The card does carry a charge of \$1.50 for ATM transactions, \$10 for a replacement card, \$15 for a paper check, and \$0.50 for denied ATM withdrawals. Block's Emerald account does not charge overdraft fees,<sup>105</sup> making it one of the safer bank account options for low-income consumers.<sup>106</sup> An important feature is that the Emerald Card is reloadable, and can receive direct deposits of a consumer's payroll.

Jackson Hewitt has its own card product, the *ipower* card. The *ipower* card costs \$30 to load for RAL or RAC, or \$10 for a holiday loan, plus any additional fees that an individual Hewitt office might charge.<sup>107</sup> The card expires sometime mid-year (July 31 for 2006 *ipower* cards), at which point Jackson Hewitt will issue a paper check, minus a \$15 close out charge.<sup>108</sup> On the other hand, the *ipower* card does not carry a fee for ATM or debit card transactions. The *ipower* card does not appear to be reloadable.

Republic Bank & Trust also has a card product. The card costs a \$30 set-up fee which includes two months of usage with 10 free ATM transactions per month, free point-of-sale purchases and free balance inquiries. There is an option to use the card as a debt card based bank account throughout the year.<sup>109</sup>

As discussed in prior years, many free tax preparation sites also partner with banks and credit unions to offer bank accounts to their unbanked clients.<sup>110</sup> Taxpayers without bank

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<sup>102</sup> Press Release, *H&R Block Announces Plan to Open 1 Million Bank Accounts for Free and Significantly Cut the Cost of Refund Lending*, H&R Block, September 7, 2006.

<sup>103</sup> *Id.*

<sup>104</sup> H&R Block Emerald Prepaid MasterCard Account Agreement, September 2006.

<sup>105</sup> Press Release, *H&R Block Announces Plan to Open 1 Million Bank Accounts for Free and Significantly Cut the Cost of Refund Lending*, September 7, 2006.

<sup>106</sup> Many banks now permit consumers to overdraw their accounts using debit/ATM cards, an abusive practice that costs consumers an estimated \$10 billion each year. See Jean Ann Fox and Patrick Woodall, *Overdrawn: Consumers Face Hidden Overdraft Charges from Nation's Largest Banks*, Consumer Federation of America, June 9, 2005, available at <http://www.consumerfed.org/pdfs/CFAOverdraftStudyJune2005.pdf>; Jacqueline Duby, Eric Halperin, and Lisa James, *High Cost & Hidden from View: The \$10 Billion Overdraft Loan Market*, Center for Responsible Lending, May 4, 2005, available at [http://www.responsiblelending.org/pdfs/ip009-High\\_Cost\\_Overdraft-0505.pdf](http://www.responsiblelending.org/pdfs/ip009-High_Cost_Overdraft-0505.pdf).

<sup>107</sup> Jackson Hewitt, *ipower CashCard Fee Schedule*, 2005.

<sup>108</sup> Jackson Hewitt, *ipower CashCard Terms and Conditions*, December 1, 2005.

<sup>109</sup> <https://www.republicrefund.com/disbursements.aspx>, last visited Jan. 30, 2007.

<sup>110</sup> NCLC/CFA 2003 RAL Report at 12-13; NCLC/CFA 2003 RAL Report at 20.

accounts cannot get direct deposit of tax refunds to avoid RALs, and may end up using commercial check cashing outlets to turn tax refunds and RALs into cash, as discussed in Section XI. A 2006 study of unbanked consumers by Scarborough Research found that 10.2 million adults lived in households that do not have any relationship with depository institutions for making financial transactions.<sup>111</sup> Unbanked consumers are more likely to be female, younger, lower-income, single and to hold blue collar occupations.<sup>112</sup> About one in twelve (8.7 percent) American families does not have a bank account, according to the latest Federal Reserve Board figures from 2004.<sup>113</sup> The figures are much higher for lower income households. Nearly a quarter (24.5 percent) of families earning in the lowest quintile (under \$18,900 annually) and about an eighth (12.7 percent) of families earning in the second lowest quintile (between \$18,900 and \$33,900 annually) do not have a transaction account.<sup>114</sup> The unbanked are also more likely to be minorities – nearly a quarter of minorities (24 percent) were unbanked compared to one in twenty (5 percent) white consumers.<sup>115</sup>

## **XI. Check Cashers and Fringe Providers Thrive during Tax Season**

Check cashers thrive during tax seasons, because cashing tax refund and RAL checks is big business. For example, ACE Cash Express has promoted a “Get Rich Quick Tax Refund Game” to lure taxpayers into its storefronts, a lottery which offers the chance to win \$25,000 a year for life to the winning customer who cashes a tax check at Ace.<sup>116</sup> The revenue from ACE’s tax refund check cashing has been rising. ACE Cash reported that tax check fees of \$21.6 million for fiscal 2006 increased by \$1.3 million over fiscal 2005 due both to larger checks and higher volume.<sup>117</sup>

A national survey of check cashing fees, products and practices, conducted during 2006 by CFA member groups, found that 94.2% of surveyed outlets cashed government checks such as tax refunds. Those outlets charged an average of 2.78% of the face value of the check to cash tax refund checks. The quoted fees ranged from 1% to 5.9% of the check.<sup>118</sup> For a \$2,500 tax refund check, the average check casher would charge \$69.50, while the most expensive outlet would charge \$147.50.

High fees to cash IRS checks are not driven by costs. The cost of cashing checks is fairly low and the risk is fairly minimal. The per-item cost to process government checks under the

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<sup>111</sup> Scarborough Research, *Unbanked Consumers: Unique Opportunities for Financial Marketers*, March 16, 2006.

<sup>112</sup> *Id.* at 4-5.

<sup>113</sup> Bucks, Brian K., Arthur B. Kennickell and Kevin B. Moore, *Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances*, Federal Reserve Bulletin, 2006 at Table 5.

<sup>114</sup> *Id.*

<sup>115</sup> Rhine, Sherrie L.W., William H. Greene and Maude Toussaint-Comeau, *The Importance of Check-Cashing Businesses to the Unbanked: Racial/Ethnic Differences*, *The Review of Economics and Statistics*, Vol. 88, No. 1, March 28, 2006 at 146-157.

<sup>116</sup> <http://www.acecashexpress.com/>, last visited Jan. 30, 2007.

<sup>117</sup> ACE Cash Express, *2006 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 69 [hereinafter “Ace 2006 Form 10-K”].

<sup>118</sup> Jean Ann Fox and Patrick Woodall, *Cashed Out: Consumers Pay Steep Premium to ‘Bank’ at Check Cashing Outlets*” Consumer Federation of America, November 2006 at 6. CFA surveyed 172 check cashing outlets in 22 states.

Federal Reserve's automated clearinghouse is about four cents.<sup>119</sup> Losses from uncollected checks are also low. The Financial Service Centers of America, the check cashers' trade association, found that less than 1 percent of checks presented to check cashers are returned and between 80 and 90 percent of those checks are ultimately collected.<sup>120</sup> Tax refund checks from the IRS and RAL checks from banks should be among the lowest risk checks.

In past reports, CFA and NCLC were critical of check cashing arrangements between H&R Block and ACE Cash Express. In fiscal 2006 ACE received \$3.1 million in tax loan check fees from the 128 self-service check cashing terminals located in H&R Block offices, down from \$3.5 million from over 130 terminals at Block stores in 2005. In 2006, ACE and Block decided to terminate that arrangement for the 2007 tax season.<sup>121</sup>

Some check cashers also sell RALs. Dollar Financial Group's Money Mart offers tax refund check cashing, tax preparation, refund estimates, e-filing, RALs from \$200 to \$9,500, Instant RALs up to \$1,800, refund anticipation checks, and "Protection Plus."<sup>122</sup> Money Mart partners with HSBC to offer RALs.<sup>123</sup>

In addition to check cashers, fringe RAL providers include used car dealers and other retailers. For example, a legal services attorney from Minnesota sent the following case study of a taxpayer who lost his refund to a used car dealer over a bad RAL deal:<sup>124</sup>

"I have a client who heard a radio advertisement stating that he could have his taxes done for free and use the money as a downpayment on a vehicle without a credit check. The paperwork he completed at the initial visit consisted of a document labeled as "refund anticipation loan," and stated that his tax refund would be \$4222, and \$3959 after fees. He also signed a paper entitled, "refund check assignment authorization" agreeing that \$3,500 would be used as a downpayment on a used vehicle. He also signed his tax forms. He did not sign any type of purchase agreement or disclosures. The dealership had difficulty obtaining the vehicle he wanted to purchase and our client said he wanted his tax refund. He was told that he had signed a contract and the refund belonged to the dealership, so of course he signed it over to them. He did not sign any further paperwork, instead his girlfriend purchased the vehicle and signed a [contract] stating the terms and listing the APR as 18.99%, when it appears that it is really 19.4%. Of course, the car is no good, and too old to be covered by any type of warranty. One thought is that my client did not receive any consideration for his tax refund."

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<sup>119</sup> Federal Reserve Bank of Richmond, 2006 Check Forward Collection Service – Richmond Office Processed at the Baltimore Office, see n. 5, effective August 1, 2006.

<sup>120</sup> Gerald Goldman and James R. Wells, *Check Cashers are Good Bank Customers*, Financial Service Centers of America, 2002, at 2. ACE Cash Express calculates that returned uncollected checks account for 0.11 percent of the company's fee revenue. Ace 2006 Form 10-K at 10. Dollar Financial calculated that net write-offs after collection accounted for 0.31 percent of the checks that were cashed. Dollar Financial Corp., *2006 Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934*, at 10.

<sup>121</sup> ACE 2006 Form 10-K at 69.

<sup>122</sup> <http://www.moneymart.com/MM/tax.asp>, last visited Jan. 30, 2007.

<sup>123</sup> [http://www.moneymart.com/MM/legal\\_info.asp](http://www.moneymart.com/MM/legal_info.asp), last visited Jan. 30, 2007

<sup>124</sup> Email from Sherry Buckner, Legal Services of Northwest Minnesota, March 8, 2006.

Some of the less well-known tax preparation websites have promoted RALs without disclosing they are loans. For example, TaxBrain.com had worked with the Internet payday lending website PRLDirect.com, to make RALs, sending an email advertising “Would you like your tax refund within 48 hours? TaxBrain.com can have your Income Tax Refund directly deposited in to your account.”<sup>125</sup>

Fringe RAL providers are also getting into the pay stub RAL business. A January 2006 ad for Casey Chevrolet states “Do Your Taxes With Your Last 2005 Pay Stub? Don’t Wait. Do It Today!”<sup>126</sup> TaxMax, a company that provides back office tax preparation services to car dealers under the name Tax Deals4Wheels, advertises that “we can calculate an estimate using a final 2006 pay stub you can sell cars while your competition waits for W-2s.”<sup>127</sup>

TaxMax also advertises that the benefits of its program include “customers can afford more expensive cars” and “taxes are prepared while they test drive your cars and you work their deals.”<sup>128</sup> And if there is any doubt that car dealers are involved in tax preparation, note that TaxMax explains in its process “salesman assists customer with tax return information.”<sup>129</sup> While TaxMax contracts with and targets car dealers as its clients, it also serves as the consumer’s tax preparer and charges the consumer \$125 for preparation services.<sup>130</sup> The RAL lender that partners with TaxMax is Santa Barbara Bank & Trust. The only page on the TaxDeals4Wheels site that specifies that the method of instantly delivering cash is actually a refund anticipation loan is the downloadable TD4W 2007 Tax Preparation Operating Agreement.

## **XII. Legislative and Regulatory Update**

There was less activity on the legislative front than in 2005, but a great deal of activity from regulators and state officials. Only one state and a municipality enacted a law regulating RALs:

### Virginia<sup>131</sup>

Virginia enacted a statute primarily focused on disclosures. The statute requires that RAL advertising conspicuously disclose that a RAL is a loan and that a fee will be charged. It also requires that RAL fees be posted in a 16 by 20 inch document in 28 point type, as well as provided in a written document. Finally, the Virginia law provides for a one-day right to rescind the loan; however, in that case, the consumer can still be charged a fee for a RAL.

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<sup>125</sup> Email from PRLDirect.com and TaxBrain.com, April 11, 2006, on file with authors.

<sup>126</sup> Advertisement from the Daily Press, January 22, 2006, on file with authors.

<sup>127</sup> [http://www.taxmax.net/td4w\\_advantage.cfm](http://www.taxmax.net/td4w_advantage.cfm), last visited January 29, 2007.

<sup>128</sup> [http://www.taxmax.net/customer\\_benefits.cfm](http://www.taxmax.net/customer_benefits.cfm), last visited January 29, 2007.

<sup>129</sup> <http://www.taxmax.net/process.cfm>, last visited January 29, 2007. In addition, TaxMax provides the car dealer with a “Taxpayer Data Sheet” and “Taxpayer Questionnaire” that appear to be forms to gather necessary information for the tax return preparation process.

<sup>130</sup> TaxMax, Taxpayer Questionnaire – Authorization to Prepare Return, October 2005, on file with authors.

<sup>131</sup> Va St. § 6.1-474.

San Antonio<sup>132</sup>

San Antonio enacted an ordinance requiring disclosure of the availability and timing of different refund options, including receiving refunds directly from the IRS. The disclosure must be made both in 14 point type and orally. The oral disclosures must be made in the language understood by the taxpayer (the taxpayer may supply the translator), and the written disclosure must be available in Spanish. In addition, like the Virginia law, the San Antonio ordinance requires a 16 by 20 inch wall posting with a fee schedule.

Also, there have been some developments with the Connecticut RAL law, which included a cap on RAL fees. The Connecticut law prohibits RAL facilitators, *i.e.*, those who broker or process RALs, from facilitating a RAL over 60% APR and imposes a fine of \$500 per violation.<sup>133</sup> The Connecticut RAL cap was struck down as preempted by the National Bank Act by a federal district court.<sup>134</sup> The case is currently on appeal to the Second Circuit Court of Appeals.<sup>135</sup>

Thus, there are currently a total of 10 states regulating RALs (California,<sup>136</sup> Connecticut,<sup>137</sup> Illinois,<sup>138</sup> Minnesota,<sup>139</sup> Nevada,<sup>140</sup> North Carolina,<sup>141</sup> Oregon,<sup>142</sup> Virginia, Washington State,<sup>143</sup> and Wisconsin<sup>144</sup>). With the exception of Connecticut, these laws primarily rely on disclosure to protect consumers from RAL abuses. While most of these laws are well-intentioned, disclosures are limited in their effectiveness in addressing the problem of RALs.

Bills that would have capped RAL interest rates were introduced but not passed in Illinois<sup>145</sup> and New York.<sup>146</sup>

On the federal level, the Senate version of the Telephone Excise Tax Repeal Act of 2005 included a number of provisions affecting RALs, which have their origins in various earlier bills introduced by Senators Bingaman and Akaka. This bill would have required registration of RAL providers, better disclosures, and funding for free tax preparation programs and bank account pilot programs to receive refunds.<sup>147</sup> It also would have eliminated the Debt Indicator and prohibited tax preparers from using tax return information for cross-marketing. These provisions

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<sup>132</sup> San Antonio City Code, §§ 16-901 to 16-907.

<sup>133</sup> Conn. Gen. Stat. § 42-480(d) and (e).

<sup>134</sup> *Pacific Capital Bank, N.A. v. Conn.*, 2006 WL 2331075 (D. Conn. Aug. 10, 2006).

<sup>135</sup> NCLC, CFA and a number of other consumer groups have filed an amicus brief in support of the State of Connecticut in this case.

<sup>136</sup> Cal. Bus. & Prof. Code § 22251 *et seq.*

<sup>137</sup> Conn. Gen. Stat. § 42-480(d) and (e).

<sup>138</sup> Ill. Comp. Stat. Ann. ch. 815, § 177/1, *et seq.*

<sup>139</sup> Minn. Stat. § 270C.445.

<sup>140</sup> Nev. Rev. Statutes, Title 52, §§ 2 to 18.

<sup>141</sup> N.C. Gen. Stat. §§ 53-245 to 53-254.

<sup>142</sup> Ore. Rev. Stat. 673.605.

<sup>143</sup> Revised Code of Washington § 19.265.010 *et seq.*

<sup>144</sup> Wis. Stat. §§ 421.301 and 422.310.

<sup>145</sup> Illinois Senate Bill 2844.

<sup>146</sup> New York A. 1994.

<sup>147</sup> S. 1321.

ultimately did not make it into the final legislation. The omnibus committee mark-up bill was not heard in the Senate.

Despite the lack of state legislative activity, state officials did not ignore RALs in 2005. The California Attorney General filed a lawsuit against H&R Block and settled a case with Jackson Hewitt, described more fully in Section XV. The New York Attorney General filed a lawsuit against H&R Block over its ExpressIRA program.<sup>148</sup> While not specifically concerning RALs, the case raised issues about another financial product sold by Block preparers.<sup>149</sup>

The State Treasurers of North Carolina, Connecticut and New York engaged in a concerted campaign to urge Block to reform its RAL practices. All three State Treasurers issued a joint statement expressing their concerns that “continuing to sell high-interest loans and marketing express IRAs to the customers least able to afford them is not only a dubious practice, but potentially places our long-term investments at risk.”<sup>150</sup> This effort occurred at the same time that the Community Reinvestment Association of North Carolina (CRA-NC) attempted to introduce a shareholder resolution on RALs at a Block annual meeting, and the Director of CRA-NC ran for the Board of Block, discussed in Section XIII.

Subsequently, the North Carolina Commissioner of Banks, along with that state’s Attorney General, and the Maryland Financial Regulation Commissioner announced investigations of tax preparers who broker RALs.<sup>151</sup> The Commissioner of Banks, Treasurer, and Governor of North Carolina unveiled a new website [www.savetherefund.org](http://www.savetherefund.org) to warn consumers of the high cost of RALs. The Governor of Wisconsin and Attorney Generals of Illinois and New Jersey issued statements warning consumers against RALs.<sup>152</sup>

The National Taxpayer Advocate devoted an entire volume in her 2007 Objectives Report to Congress on RALs.<sup>153</sup> This came on the heels of her inclusion of RALs as the eighth most serious problem facing taxpayers in her 2005 Annual Report to Congress.<sup>154</sup> The National Taxpayer Advocate’s 2007 Objectives Report made a number of recommendations to reform RAL practices, including (1) improving IRS oversight of tax preparers who are authorized to file

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<sup>148</sup> Complaint, *People v. H&R Block*, (N.Y. Supreme Court March 15, 2006), available at <http://www.oag.state.ny.us/press/2006/mar/H%20%20R%20BLOCK%20COMPLAINT.pdf>

<sup>149</sup> It has also led to a number of private class actions against Block. See *In re H&R Block, Inc. Express IRS Marketing Litigation*, 444 F. Supp.2d 1339 (Jud. Pan. Mult. Lit. 2006)

<sup>150</sup> Letter from NC Treasurer Richard Moore, NY Treasurer Alan Hevesi, and CT Treasurer Denise Nappier to Mark Ernst, August 15, 2006, available at <http://www.state.ct.us/ott/pressreleases/press2006/pr081506letter.pdf>; see also Mike Baker, *States Blast H&R Block Over High Interest Loans*, Associated Press, August 16, 2006; Frank Norton, *States Criticize H&R Block*, Charlotte News & Observer, August 16, 2006.

<sup>151</sup> Christopher D. Kirkpatrick, *Scrutiny for Loans Tied to Tax Refunds: NC Investigates Whether Offerings Break State Lending Laws*, Charlotte News & Observer, November 15, 2006; *Md. Regulators Launch Inquiry into Tax Refund Loans*, Washington Business Journal, January 10, 2007.

<sup>152</sup> Press Release, *Refund Anticipation Loans: A High Price to Pay to Borrow Your Own Money*, Wisconsin Department of Revenue, January 9, 2006; Press Release, *Consumers Cautioned About Tax Refund Anticipation Loans*, New Jersey Attorney General’s Office, April 10, 2006; Press Release, *Madigan Warns Consumers: With Tax Season Nearing Its End, Don’t be Fooled by Refund Anticipation Loans*, Illinois Attorney General’s Office, March 31, 2006.

<sup>153</sup> National Taxpayer Advocate, *2007 Objectives Report to Congress: Volume II – The Role of the IRS in the Refund Anticipation Loan Industry*, June 30, 2006 [hereinafter “National Taxpayer Advocate 2007 Objectives Report”].

<sup>154</sup> National Taxpayer Advocate 2005 Report to Congress at 162-179.

electronically (electronic return originators); (2) eliminating the ability of preparers to have an ownership interest in RALs; (3) issuing refunds to the unbanked using prepaid cards; (4) speeding up IRS issuance of refunds; (5) enacting legislation to prohibit cross-lender debt collection of RALs; (6) providing a Revenue Protection Indicator when the IRS acknowledges receipt of a-filed return; and (7) amending IRC Section 7216 to prohibit use of tax return information for non-tax purposes (including RALs).<sup>155</sup>

Finally, the IRS released its report to Congress, as required by H.R. 3058 (2006), § 221.<sup>156</sup> NCLC and CFA submitted extensive information to the IRS for this report, yet the report was never released to the general public, including consumer groups. The report attempts to represent the positions of the stakeholders in the RAL debate in a “fair and balanced fashion”,<sup>157</sup> and uses the study by the Credit Research Center at Georgetown University (CRC) to provide the industry perspective. However, the IRS report never mentions the fundamental flaw of the CRC study, that it grossly underestimates the percentage of RAL borrowers and only reached about one-quarter of them because it specifically asked survey respondents whether they had ever taken out a “refund anticipation loan” which it specified as “a loan or advance of money against a tax refund, typically provided by a bank,” yet many RAL borrowers are not aware the product is a bank loan.<sup>158</sup>

The IRS makes few recommendations as to reforming RALs, claiming “primary regulatory oversight of RALs is provided in the banking law and therefore not administered by IRS” and “RALs are loans placing them outside the direct regulatory authority of the IRS.”<sup>159</sup> It disputes some of the National Taxpayer Advocate’s analysis and recommendations as to what the IRS could do with respect to RALs, especially with respect to oversight of tax preparers. The IRS ignored the critical role of the tax preparer in brokering RALs – the preparer solicits the customers, collects the borrowers’ information, fills in the loan applications, prints out the loan agreements, and even issues the loan checks.<sup>160</sup> The preparer is often the only point of contact between the taxpayer and the bank lender regarding the RAL.

The IRS report also criticizes use of the APR to express the cost of a RAL, buying into an argument often used by RAL lenders (and payday lenders) that the APR is not the “real interest rate that taxpayers are charged” because it is calculated on an annualized basis yet the loan fee is a flat amount.<sup>161</sup> This position is faulty because it considers only periodic interest – and periodic interest computed as simple interest - to be the “real interest rate” of a loan. Yet the true cost of credit for a loan often is not comprised solely of simple interest; in fact, the reason why Congress enacted the Truth in Lending Act over thirty years ago was because “interest” can be expressed in so many confusing (and deceptive) ways.<sup>162</sup> The IRS’s position also ignores the time factor in

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<sup>155</sup> National Taxpayer Advocate 2007 Objectives Report at 18-19.

<sup>156</sup> IRS, Report to Congress, November 2006.

<sup>157</sup> *Id.* at 1.

<sup>158</sup> For a further discussion of the flaws of the CRC study, see Appendix A to the 2006 NCLC/CFA Report.

<sup>159</sup> IRS, Report to Congress, November 2006 at 2, 8.

<sup>160</sup> *See, e.g.*, Plaintiff’s Local Rule 56(a)(1) Separate Statement of Undisputed Facts at ¶¶4-6, *Pacific Capital Bank, N.A. v. Conn.*, No. 3:06-CV-28 (D. Conn. Aug. 10, 2006).

<sup>161</sup> IRS, Report to Congress, November 2006 at 12.

<sup>162</sup> *See* National Consumer Law Center, *Truth in Lending*, § 1.1.1 (5<sup>th</sup> ed. 2003 and Supp.) (discussion of the legislative history of the Truth in Lending Act). The IRS analysis also fails to recognize that even simple interest is



expressing the cost of credit when a flat fee is involved, which is critically important. As one commentator has remarked, interest on a loan is like the rent for borrowing money. To analogize to a real estate rental, \$15,000 may be a reasonable rent for an apartment for one year, but it is an expensive rental for one week.

The primary position staked out by the IRS in its Report to Congress was to support continuation of the Debt Indicator.<sup>163</sup> The IRS noted that the Debt Indicator prevents taxpayers from defaulting on RALs.<sup>164</sup> While this may be true, the IRS did not discuss the countervailing reasons to terminate the Debt Indicator – that it also increases RAL volume and RAL profits (due to the fact that the promised drop in prices in exchange for its reinstatement quickly vanished after a year),<sup>165</sup> and the sheer impropriety of the IRS using government resources to help RAL lenders and loan brokers in making these abusive loans. The National Taxpayer Advocate has proposed an innovative compromise to the issue. She proposed that the IRS provide a “Revenue Protection Indicator” which would delay release of the acknowledgement file (indicating acceptance of an e-filed return) until the IRS had run the taxpayer’s return through several compliance screens in order to ensure that the refund will not be delayed or reduced by compliance actions.<sup>166</sup> This would delay issuance of RALs and make them less attractive to consumers and lenders.

### **XIII. Anti-RAL Advocacy**

This past year saw a bumper crop of anti-RAL advocacy by state and regional consumer groups across the country, much of it actively coordinated. These efforts included groups in California (California Reinvestment Coalition (CRC)), Illinois (Woodstock Institute and Center for Economic Progress), New York City (Neighborhood Economic Development Advocacy Project (NEDAP)), North Carolina (Community Reinvestment Association of North Carolina (CRA-NC)) and Philadelphia (Community Legal Services and the Campaign for Working Families). For example:

- CRA-NC, NEDAP, CRC, Woodstock Institute, and New Jersey Citizen Action held a joint protest in front of Jackson Hewitt’s headquarters in Parsipanny, New Jersey to demand that Jackson Hewitt end abusive RAL lending practices. To demonstrate their demand, they presented a 3-foot by 5-foot 'rapid refund' check in the amount of \$74.5 million for Jackson Hewitt CEO & President Michael Lister to sign, made payable to The

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not the only way to calculate periodic interest. Periodic interest can be calculated as add-on interest or a discount rate. Each method results in a different amount paid by the consumer as “real interest”. For example, a \$6,000 car financed at a 6% interest rate for 3 years can result in paying \$969.72 as simple interest, \$1080 as add-on interest, or \$1317.06 using a discount rate! *Id.*

<sup>163</sup> IRS, Report to Congress, November 2006 at 15-18; National Taxpayer Advocate 2007 Objectives Report at 8-10.

<sup>164</sup> Interesting, the IRS notes that the Debt Indicator prevented 844,569 taxpayers from obtaining and then defaulting on RALs. These taxpayers applied for RALs based on \$429 million of refunds that they never received due to an offset. IRS, Report to Congress, November 2006 at 16. That works to about \$500 per taxpayer, which is a far smaller refund than the average refund – indicating that taxpayers who were prevented from getting a RAL by the Debt Indicator had smaller refunds than the average taxpayer.

<sup>165</sup> See Chi Chi Wu, *Corporate Welfare for the RAL Industry: the Debt Indicator, IRS Subsidy, and Tax Fraud*, National Consumer Law Center, at 1 (July 2005).

<sup>166</sup> National Taxpayer Advocate 2007 Objectives Report at 12.

Working Families of America. The check represented the amount of money Jackson Hewitt drained from consumer's refunds through its brokering of RALs in 2006.<sup>167</sup>

- The Community Reinvestment Association of North Carolina attempted to introduce a shareholder resolution on RALs at a Block annual meeting. The SEC ultimately permitted Block to avoid a vote on the resolution. Peter Skillern, the Executive Director of CRA-NC, ran as a candidate for the H&R Block Board of Directors. While not elected as a Director, Skillern did use Block's Annual Meeting of shareholders as a platform to urge the company to support a ban on RALs.<sup>168</sup> In addition, CRA-NC provided assistance to the North Carolina Treasurer's efforts, discussed in Section XII above.
- Community Legal Services (CLS) and the Campaign for Working Families (CWF) in Philadelphia sent undercover testers to Block and Jackson Hewitt offices in February 2006. They found that Block and Hewitt personnel failed to comply with company-mandated RAL disclosures, to adequately explain refund options, to provide price quotes for tax preparation, and were operating illegally as unlicensed loan brokers.<sup>169</sup> The Hewitt preparer automatically included a RAL, while the Block preparer aggressively pushed an "Instant Check" (i.e., same day RAL). The Hewitt preparers also failed to give proper Truth in Lending disclosures.

CLS and CWF subsequently sent testers to Block and Hewitt offices to investigate pay stub RALs offered by both companies. CLS and CWF worked with a local news station to send a "hidden camera" to those offices. The testing documented several problems with the pay stub RAL process, including wildly varying estimates of refunds based on pay stubs (\$4,000 versus \$5,700), steering or requiring taxpayers to use future preparation services, and requiring clients to sign up for dummy bank account products at additional cost.<sup>170</sup>

- The California Reinvestment Coalition (CRC) organized a protest and press conference in front of a Block office in Oakland, CA.<sup>171</sup> The protest included representatives of a number of California organizations.
- The Woodstock Institute, Center for Economic Progress, and Illinois Legal Aid held a press conference spotlighting the abuses of Jackson Hewitt pay stub and holiday RALs.<sup>172</sup>

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<sup>167</sup> Press Release, *Groups From Five States Demand that Jackson Hewitt End Abusive Lending Practices*, CRA-NC, NEDAP, CRC, Woodstock Institute, and New Jersey Citizen Action, January 16, 2006.

<sup>168</sup> Mark Davis, *Dark Horse Eyes Block Job*, Kansas City Star, September 1, 2006.

<sup>169</sup> Letter to H&R Block Chairman Mark Ernst from Community Legal Services, April 4, 2006; Letter to Jackson Hewitt Chairman Michael Lister from Community Legal Services, April 4, 2006.

<sup>170</sup> Nydia Han, *Pitfalls of a Tax Day Loan*, WPVI-TV, January 16, 2006; Press Release, *Consumers Alerted to Earlier-Than-Ever Tax Time Rip-Offs*, Campaign for Working Families, January 17, 2007.

<sup>171</sup> Francine Brevetti, *Activists Protest H&R Block Policy*, Oakland Tribune, February 23, 2006.

<sup>172</sup> Press Release, *Grinch is No HELP At All: Major Tax Preparers Offer Expensive New Holiday Tax Loans Consumer Groups Push Back*, Woodstock Institute, Center for Economic Progress, and Illinois Legal Aid Online, November 21, 2006.

- ACORN targeted Money Mart over a number of high cost financial services, including RALs as well as payday loans and check cashing fees.<sup>173</sup>

Some of these groups, as well as other advocacy organizations, issued reports on RALs, including:

- Chris Keeley, Sarah Ludwig and Mark Winston Griffith, *Predatory Tax-Time Loans Strip \$324 Million From New York City's Poorest Communities: An Analysis of Tax Refund Anticipation Lending in NYC 2002 – 2005*, Neighborhood Economic Development Advocacy Project, January 2007, available at <http://www.nedap.org/documents/FINAL2007NEDAPRALsreport.pdf>.
- Peter Skillern and Adam Rust, *The High Cost of Refund Anticipation Loans in North Carolina*, CRA-NC, January 25, 2007, available at <http://www.cra-nc.org/New%20web%20content/2006%20RALReport01.pdf>.
- Tom Feltner, *Refund Anticipation Loans Usage Rates Negatively Impact the Asset Building Potential of the Earned Income Tax Credit*, Reinvestment Alert No. 29, Woodstock Institute, February 2006, available at <http://www.woodstockinst.org/document/alert29.pdf>.
- David Rothstein, *Credit Where It's Due: The Earned Income Tax Credit in Ohio*, Policy Matters Ohio, March 2006, available at [http://www.policymattersohio.org/pdf/credit\\_where\\_its\\_due.pdf](http://www.policymattersohio.org/pdf/credit_where_its_due.pdf).
- ACORN Financial Justice Center, *Missing Millions: Expanding Access to the Earned Income Tax Credit While Reducing Reliance on Refund Anticipation Loans*, ACORN, January 2007, available at [http://www.acorn.org/fileadmin/ACORN\\_Reports/2007/EITC2007.pdf](http://www.acorn.org/fileadmin/ACORN_Reports/2007/EITC2007.pdf).
- *Keeping What They've Earned: Working Americans and Tax Credits*, Children's Defense Fund (February 2006) (versions for California, District of Columbia, Mississippi, Ohio, South Carolina, Tennessee, and Texas), available at [http://www.childrensdefense.org/site/PageServer?pagename=research\\_family\\_income](http://www.childrensdefense.org/site/PageServer?pagename=research_family_income).
- Children's Defense Fund Minnesota, *Keeping What They've Earned: Working Minnesotans and Tax Credits* (February 2006), available at [http://www.cdf-mn.org/PDF/EITC\\_RAL\\_report\\_06\\_3.pdf](http://www.cdf-mn.org/PDF/EITC_RAL_report_06_3.pdf).

Finally, there are a number of free tax preparation programs across the country that are providing low-cost alternative RALs, including Alternatives Credit Union in Ithaca, NY, AccountAbility Minnesota, and San Antonio, TX.

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<sup>173</sup> Press Release, *ACORN Gives Money Mart "Loan Shark of the Year" Award*, ACORN, February 3, 2006.

#### XIV. RAL Lending to Service Members

The men and women of our armed forces are a prime target market for RALs, according to a report on predatory lending prepared by the Department of Defense (DOD) for Congress in 2006.<sup>174</sup> A survey conducted as part of the DOD report (the Defense Manpower Data Center Active Duty Survey) found that 4% of all Service members reported taking out a RAL in 2006. Since the survey asked Service members whether they had gotten a “loan” and many consumers who get RALs are unaware of their nature of as a loan, this self-reported information likely understates the number of Service members using RALs.<sup>175</sup> NCLC and CFA estimate from IRS data that 7.5% of Service members received refund anticipation loans in 2005. If so, Service members paid \$10,027,290 to borrow against their tax refunds.<sup>176</sup>

In 2006, Congress enacted the John Warner Defense Authorization Act of 2007, which includes protections against predatory lending to active duty Service members (the “Military Lending Act”). The new law, which takes effect October 1, 2007, caps rates for loans to the military at 36% APR including fees and insurance premiums. DOD will be issuing regulations to implement the new law. Unfortunately, banks have been arguing to DOD that they should be given a blanket exemption from the Military Lending Act’s 36% APR usury cap. CFA and NCLC believe the Military Lending Act’s 36% APR cap should apply to loans by banks, including RALs that are facilitated by tax preparers. RALs cost 40% to 500% APR, depending on the size of the loan. If document processing or applications fees are charged and computed in the APR as required by the Military Lending Act, RALs cost 57% to 1,100% APR which should violate the Act next tax season, depending on DOD regulations.

Service members should be protected from predatory RAL lending by the Military Lending Act, because they are a prime target for tax preparers and other businesses who promote and facilitate these loans. Data from two states show that these businesses cluster around military bases in a pattern similar to the distribution of payday lenders.<sup>177</sup>

Dr. Steven Graves of California State University at Northridge provided us with an analysis of the incidence of RAL providers in Washington and North Carolina, two states that require RAL facilitators to register with state regulators. Dr. Graves prepared maps showing the incidence of RAL facilitators based on population per ZIP code area. These maps, which are attached as Appendix A to this report, demonstrate that RAL lenders near military bases have more locations than population alone would justify. The municipality of Lakewood, WA, near Ft.

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<sup>174</sup> Department of Defense, *Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents*,] August 9, 2006, at 20.

<sup>175</sup> See NCLC/CFA 2005 RAL Report at 7-8. An NCLC poll found that 70% of RAL users did not realize they had received a loan, with younger consumers least likely to know a RAL was a loan. A CFA poll found that RAL borrowers are heavier users than non-RAL borrowers of other high cost fringe financial services, such as rent-to-own, payday loans, and pawnshop loans. See NCLC/CFA 2006 RAL Report at 10.

<sup>176</sup> These totals are calculated assuming an average refund of \$2,500, with RAL fees of \$100. If additional fees charged by some tax preparers who facilitate RALs are included, the total would be higher. See Section II above.

<sup>177</sup> Steven M. Graves and Christopher L. Peterson, *Predatory Lending and the Military: The Law and Geography of ‘Payday’ Loans in Military Towns*, 66 Ohio State Law Journal 4 (2005).

Lewis, has a substantial concentration of RAL facilitators (as well as payday lenders).<sup>178</sup> Four of the ten most over-represented ZIP codes for RAL facilitators in Washington are within a few miles of McCord/Ft. Lewis military complex. Lakewood has eleven more RAL outlets than population supports.

For each of the North Carolina military bases, adjacent ZIP code areas have higher than expected RAL outlets based on population. Ft. Bragg's Fayetteville ZIP is among the three most over-represented ZIP codes in the state with 15 more RAL outlets than would be expected based on its population. Jacksonville, next to Camp LeJeune, has nine more RAL facilitators than expected while Goldsboro, near Seymour Johnson Air Force Base, has 5.5 extra RAL outlets.

The same pattern of heavy RAL lending around military bases occurs in New York. The Neighborhood Economic Development Action Project (NEDAP) mapped refund anticipation loans by ZIP Code for 2002 through 2005.<sup>179</sup> An analysis of NEDAP's maps shows that a tax return filed at or around a military installation in New York State is nearly four times more likely to have a RAL than a tax return filed elsewhere in New York. For the two ZIP Codes near Fort Drum, NY, almost 28 percent of tax returns included a RAL, compared to 7.5 percent statewide. RAL borrowers in the 13602 and 13603 ZIP Codes near Fort Drum spent \$1,629,638 in fees to borrow against tax refunds during that four-year period.<sup>180</sup>

Military personnel who have access to free tax preparation assistance through the IRS VITA program on base can take advantage of free tax preparation without costly loans based on anticipated refunds. Since over 92% of Service members using VITA sites were reported to have bank or credit union accounts, they can almost all benefit from direct deposit of tax refunds. The IRS reports data from military personnel whose taxes are prepared at VITA sites on base. Over 320,000 Service members and retirees filed their taxes through these free military VITA sites in 2005, claiming refunds worth \$531,781,767, and about 83% of them received their refunds by direct deposit.<sup>181</sup> There were over 1.3 million active duty Service members at the end of 2005.<sup>182</sup> Even assuming that all of the Military VITA site filers were active duty, less than a fourth of active duty Service members took advantage of free tax preparation and filing services on their bases in 2005.

The IRS data also shows that for Service members who did use a military VITA site, many of them claimed both the EITC and Child Tax Credit. This indicates an appreciable population of EITC and CTC recipients among Service members, and that the Service members

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<sup>178</sup> DOD reported to Congress that there are four times as many payday lenders per capita near McChord Air Force Base and Fort Lewis compared to residents living in the rest of Washington State. See Gordon Trowbridge and Karen Jowers, *Payday Predators*, Army Times, May 2, 2005, at 4.

<sup>179</sup> Chris Keeley, Sarah Ludwig and Mark Winston Griffith, *Predatory Tax-Time Loans Strip \$324 Million From New York City's Poorest Communities: An Analysis of Tax Refund Anticipation Lending in NYC 2002 – 2005*, Neighborhood Economic Development Advocacy Project, January 2007, available at <http://www.nedap.org/documents/FINAL2007NEDAPRALsreport.pdf>

<sup>180</sup> NEDAP, *Military Personnel Targeted by Tax Refund Anticipation Lending in NYS, 2002-2005*, on file with author, January 2007.

<sup>181</sup> Data from IRS SPEC, Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.

<sup>182</sup> DefenseLink website noted 1,336,972 active duty Service members as of December 31, 2005, <http://siadapp.dior.whs.mil/personnel/MILITARY/rg0512.pdf> as reported in the DOD Report to Congress.

who do not use VITA sites may be losing a portion of their credits to RALs and other fees. Over twelve percent of Service members at Military VITA sites filed returns with EITC received worth \$60,443,134.<sup>183</sup> Almost 25 percent of them claimed the child tax credit worth \$101,402,731, plus additional child tax credits worth another \$60,662,161. Five percent filed returns with both a child tax credit and EITC received.<sup>184</sup>

## **XV. Litigation**

A major settlement was reached this year in RAL class actions, while the California Attorney General took aggressive enforcement action against H&R Block and Jackson Hewitt over RALs.

### Carnegie v. Household International<sup>185</sup>

The third time was the charm for settling this nationwide class action with a tortured history that included two rejected settlement attempts. A federal district court finally approved a settlement, which includes \$30 million in cash to the class, \$7.75 million to class attorneys, and \$2 million for administration costs. More importantly, the settlement did not include coupons and did not attempt to snuff out any viable class actions brought against Block and Household/HSBC.

### California Attorney General Cases

The California Attorney General filed a lawsuit against H&R Block in February 2006, alleging that Block made misleading statements in its promotion of its RAL and RAC program. The California Attorney General also challenged Block's cross-lender debt collection practices and alleged violation of IRS privacy rules regarding sharing of information for cross-marketing.<sup>186</sup> Block attempted to remove this lawsuit from state court into federal court, but the federal court ordered the case sent back.<sup>187</sup>

The California Attorney General also filed a lawsuit against Jackson Hewitt, alleging similar abuses. Jackson Hewitt agreed to enter into a settlement with the Attorney General, promising reforms of its practices and paying \$4 million in consumer refunds plus \$1 million in penalties and costs.<sup>188</sup>

### Hood v. Santa Barbara Bank & Trust

*Hood v. SBBT*<sup>189</sup> is a class action challenging cross-lender debt collection under California's debt collection and unfair trade practices laws. NCLC is co-counsel for the

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<sup>183</sup> Data from IRS SPEC, Return Information Database for Tax Year 2004 (Returns Filed in 2005), November 2006.

<sup>184</sup> *Id.*

<sup>185</sup> *Carnegie v. Household International*, 445 F.Supp.2d 1032 (N.D. Ill. 2006).

<sup>186</sup> Complaint, *People of California v. H&R Block, Inc.* (Cal. Sup. Ct. San Francisco Feb. 15, 2006), available at [http://ag.ca.gov/newsalerts/cms06/06-013\\_0a.pdf](http://ag.ca.gov/newsalerts/cms06/06-013_0a.pdf).

<sup>187</sup> *People of California v. H&R Block*, 2006 WL 2669045 (N.D. Cal. Sep. 18, 2006).

<sup>188</sup> Judgment, *People of the State of California v. Jackson Hewitt*, Case No. 070304558 (Cal. Sup. Ct. Alameda Cty Jan. 3, 2007), available at [http://ag.ca.gov/cms\\_pdfs/press/2007-01-03\\_Jackson\\_Hewitt\\_Settlement\\_Judgment.pdf](http://ag.ca.gov/cms_pdfs/press/2007-01-03_Jackson_Hewitt_Settlement_Judgment.pdf)

<sup>189</sup> See Complaint, *Hood v. Santa Barbara Bank & Trust*, Case No. 1156354 (Cal. Super. Ct. County of Santa Barbara March 18, 2003), available at [www.consumerlaw.org/initiatives/refund\\_anticipation](http://www.consumerlaw.org/initiatives/refund_anticipation).

putative class in this case. In September 2006, the California Court of Appeals reversed the dismissal of the plaintiffs' claims against SBBT on the basis of federal preemption under the National Bank Act.<sup>190</sup>

RAL litigation appears to continue against the major commercial chains. For example, a consumer class action was brought against a major Jackson Hewitt franchisee in New York City.<sup>191</sup> Lawsuits have been brought against Jackson Hewitt for violation of state credit services organization acts.<sup>192</sup>

There could be other potential litigation in the future. For example, last year, SBBT dropped a surcharge from RALs secured by EITC refunds. This surcharge arguably violated the Equal Credit Opportunity Act (ECOA), 15 U.S.C. §§ 1691–1691f, which prohibits discrimination in lending against public assistance recipients. SBBT also recently changed its loan agreements to provide an option for a RAL applicant's spouse to indicate they do not accept personal liability for the RAL. This may have been changed to also comply with the ECOA, which prohibits creditors from requiring the spouse of a credit applicant to co-sign a loan.<sup>193</sup>

## **XVI. Tax Return Privacy**

In 2006, the IRS rules for Section 7216 of the IRS Code, which govern the disclosure and use of tax returns by tax preparers, underwent a highly publicized review.<sup>194</sup> The IRS proposed rules that would eliminate a provision that consumer groups believe restricts the use of tax return information for cross-marketing by companies unaffiliated with the tax preparer. Current rules permit consumers' tax return information to be used by tax preparers to market only their own products or products offered by their affiliates. A separate written consent form must be signed for each use of tax return information.

Under the proposed rules, tax preparers will be permitted to share (or even sell) the contents of a consumer's entire tax return with an unaffiliated business in order to solicit the consumer for commercial products, provided the consumer signed a consent form. Once the taxpayer's information was in the hands of the third party, IRS privacy rules would no longer apply and information could be used without further consent. Consumers were shocked to learn from news reports that current and proposed rules exposed their personal information to privacy and security risks.

NCLC, CFA, and PennPIRG filed comments and presented testimony opposing the proposed weakening of privacy rules and urged the IRS to eliminate the current sharing of

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<sup>190</sup> *Hood v. Santa Barbara Bank & Trust*, 49 Cal.Rptr.3d 369 (Cal. Ct. App. 2006).

<sup>191</sup> Susan Edelman, *Firm's Tax-Free Scams: Jackson Hewitt Suit*, New York Post, November 19, 2006.

<sup>192</sup> *See, e.g.*, *Brailsford et al. v. Jackson Hewitt Inc.*, Case No. C-06-00700-CW (N.D. Cal. 2006).

<sup>193</sup> Regulation B, 12 C.F.R. § 202.7(d). *See* National Consumer Law Center, *Credit Discrimination*, § 5.6 (4th ed. 2006 and Supp.).

<sup>194</sup> IRS, Notice of Proposed Rulemaking, Guidance Necessary To Facilitate Electronic Tax Administration - Updating of Section 7216 Regulations, 70 Fed. Reg. 72954 (December 8, 2005). Comments of NCLC, CFA and PIRG to the IRS re: Notice of Proposed Rulemaking Amendments to Section 7216 Regulations and Revenue Guidance, March 8, 2006, available at [www.consumerfed.org/pdfs/IRS\\_Privacy\\_Rule\\_Comments.pdf](http://www.consumerfed.org/pdfs/IRS_Privacy_Rule_Comments.pdf).

information with tax preparer affiliates.<sup>195</sup> The National Association of Attorneys General and individual Attorneys General from North Carolina and Minnesota filed comments opposing the proposed rule changes. A public hearing was held in April 2006, but the IRS has yet not issued final rules.

Tax returns are a gold mine of personal and financial information, including Social Security numbers, income and investments, names and addresses of family members, bank and credit card account numbers. The specter of tax return information sharing raises serious concerns about data security, identity theft, unwarranted marketing including to children, privacy invasion, and loss of confidence in the largely voluntary filing of tax returns. The trust relationship between a consumer and a tax preparer in combination with the complexity of tax return preparation, and the multiple pages that must be signed, make it likely that a consumer could unknowingly sign a consent for tax return information sharing.

Tax return data sharing is an essential element of RAL processing. During the loan approval process, the taxpayer's return information is sent by the tax preparer to the lending bank. As the Minnesota Attorney General told the IRS, "tax preparers and their affiliates now regularly rely on the current cross-marketing regulations to pitch products and services of questionable utility, including, in particular, refund anticipation loans, individual retirement accounts, and sub-prime mortgage loans offered to low-income consumers with onerous fees and interest rates."<sup>196</sup>

Numerous bills were filed in Congress in 2006 in reaction to publicity about the IRS proposed privacy rules, as well as flaws in the current rules. Several House bills<sup>197</sup> prohibited disclosure or use of tax return information even with taxpayer consent while Senate bills<sup>198</sup> prohibited disclosure or use of tax return information only to third parties. None of the taxpayer privacy and security bills have yet been enacted.

Whether tax preparers comply with current data privacy rules was challenged in the California Attorney General's lawsuits against H&R Block and Jackson Hewitt. Both companies were accused of failing to get proper consent from California RAL borrowers to use or disclose tax return information to RAL-lending banks for purposes of providing RALs and other financial products and for purposes of collecting prior RAL debts or allowing others to collect such debts.<sup>199</sup> Jackson Hewitt settled with the Attorney General, discussed further in Section XV. In settling the case, Jackson Hewitt agreed to reform its information sharing and consent forms by providing a stand-alone document for each proposed use or disclosure of tax return information.

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<sup>195</sup> *Id.*; Testimony of Beth McConnell, Director, Pennsylvania Public Interest Group Education Fund before the Internal Revenue Service Public Hearing, April 4, 2006, available at <http://pennpirg.org/PA.asp?id2=23263>.

<sup>196</sup> Mike Hatch, Minnesota Attorney General, Letter to IRS Commissioner Mark W. Everson, Re: REG-137243 and Notice 2005-93, March 28, 2006 at 2.

<sup>197</sup> H. R. 5063 by Rep. Chet Edwards, H. R. 5075 by Rep. Pete Stark, H. R. 5084 by Rep. John Dingell, and H.R. 5138 by Rep. J. D. Hayworth.

<sup>198</sup> S. 2484 by Senators Obama, Menendez, Harkin, Clinton and Lieberman; S. 2498 by Senator Thomas.

<sup>199</sup> Complaint, People of the State of California v. Jackson Hewitt, Case No. 070304558 (Cal. Sup. Ct. Alameda Cty Jan. 3, 2007), available at [http://ag.ca.gov/cms\\_pdfs/press/2007-01-03\\_Jackson\\_Hewitt\\_Complaint.pdf](http://ag.ca.gov/cms_pdfs/press/2007-01-03_Jackson_Hewitt_Complaint.pdf); Complaint, People of California v. H&R Block, Inc. (Cal. Sup. Ct. San Francisco Feb. 15, 2006), available at [http://ag.ca.gov/newsalerts/cms06/06-013\\_0a.pdf](http://ag.ca.gov/newsalerts/cms06/06-013_0a.pdf).



Jackson Hewitt will be required to bind third party recipients of information not to use or share information for any other purpose.<sup>200</sup>

## **XVII. Reform**

The following reform proposals are based upon a modified version of the National RAL Platform: Issues and Options, first discussed in the NCLC/CFA 2005 RAL Report and available at [www.consumerlaw.org/action\\_agenda/refund\\_anticipation/content/RALplatform.pdf](http://www.consumerlaw.org/action_agenda/refund_anticipation/content/RALplatform.pdf). We have modified some of the proposed options due to recent events.

### *A. Options for Federal Legislation*

1. Ban RALs.
2. Cap RAL fees.
3. Establish a licensing scheme for tax preparers and/or facilitators.
4. Prohibit or regulate abusive features of RALs, including:
  - a. debt collection by set-off of a tax refund.
  - b. mandatory arbitration clauses.
5. Modify IRS administrative goals re: reaching the 80% e-file rate.
6. Require better disclosures on RALs, including:
  - a. mandatory warning language and text size
  - b. wall postings
  - c. amend the Truth in Lending Act to prohibit unbundling of fees, so that the disclosed APR reflects the true costs of getting a RAL.
7. Dramatically simplify tax code for low-income filers.
8. Fund “banking the unbanked” programs.
9. Make free electronic filing directly with the IRS available to all taxpayers.

### *B. Options for State or Local Regulation*

1. Cap RAL fees by regulating facilitators or prohibiting them from earning any compensation for brokering RALs.
2. Impose a duty on return preparers to act in the best financial interests of their customers.
3. Establish a registration scheme for RAL facilitators.
4. Require better disclosures on RALs, including:
  - a. mandatory warning language.
  - b. wall postings.
  - c. require disclosure of special “RAL interest rate” that includes all RAL fees.
5. Regulate advertising of RALs.
6. Prohibit or regulate abusive features of RALs, including:
  - a. debt collection by set-off of a tax refund.
  - b. certain aspects of mandatory arbitration clauses.

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<sup>200</sup> Judgment, *People of the State of California v. Jackson Hewitt*, Case No. 070304558 (Cal. Sup. Ct. Alameda Cty Jan. 3, 2007), available at [http://ag.ca.gov/cms\\_pdfs/press/2007-01-03\\_Jackson\\_Hewitt\\_Settlement\\_Judgment.pdf](http://ag.ca.gov/cms_pdfs/press/2007-01-03_Jackson_Hewitt_Settlement_Judgment.pdf).

- c. referrals to check cashers or permitting check cashing on the premises.
- 7. Regulate check cashing fees for RALs and refund checks.
- 8. No RALs based on state tax refunds.

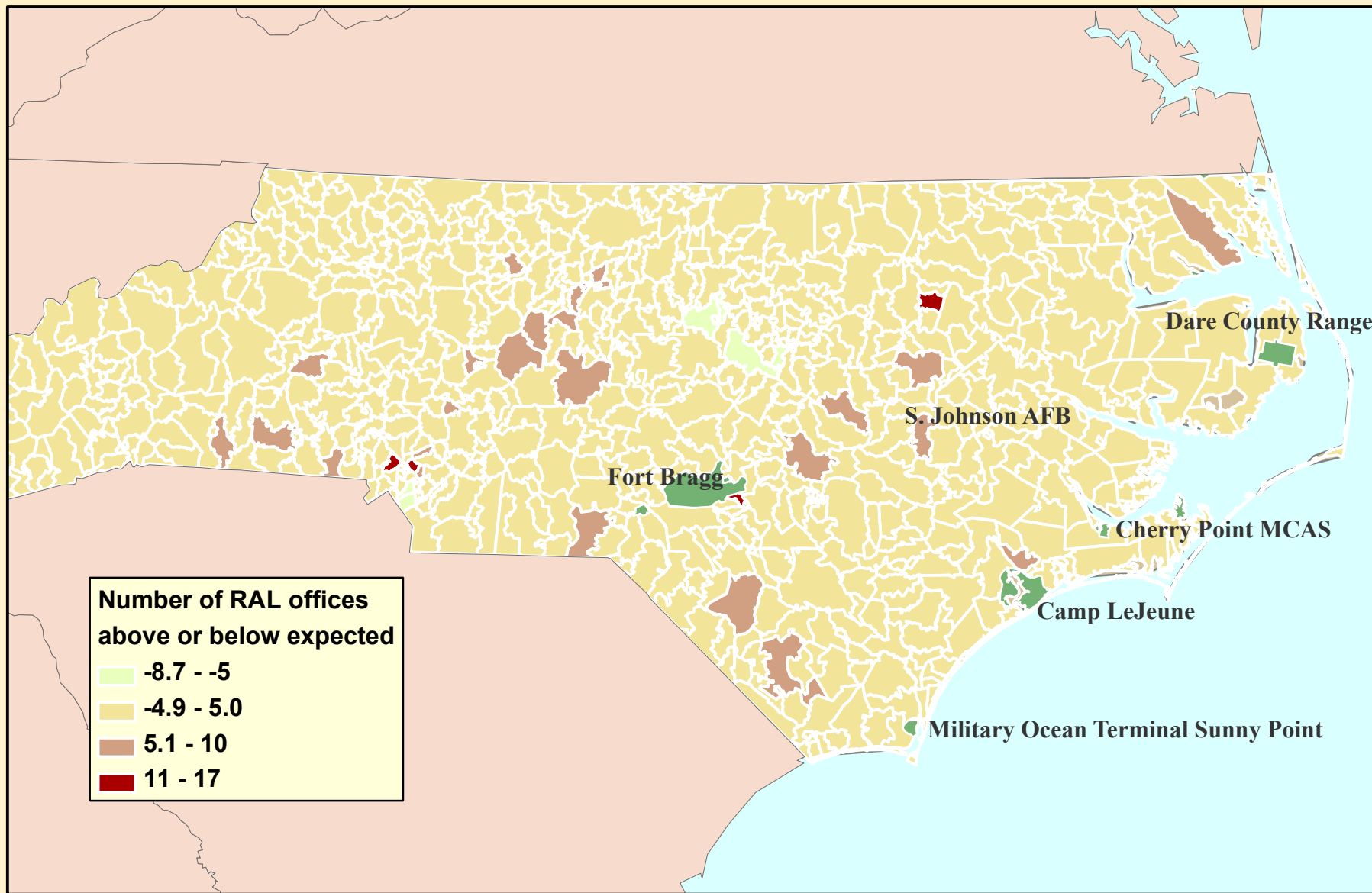
*C. Options for Treasury/IRS Administrative Action*

- 1. Speed IRS refund turnaround time to 48–72 hours.
- 2. Eliminate the Debt Indicator program or institute a Revenue Protection Indicator.<sup>201</sup>
- 3. Improve and expand the Advance EIC.
- 4. Strengthen IRS privacy regulations to prohibit use of taxpayer information to cross-market financial products.
- 5. The Federal Reserve Board should apply the consumer protections of the Electronic Funds Transfer Act to stored value card products that receive tax refund or RAL proceeds.

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<sup>201</sup> As proposed by the National Taxpayer Advocate, described in Section XII above.

## **APPENDIX A**



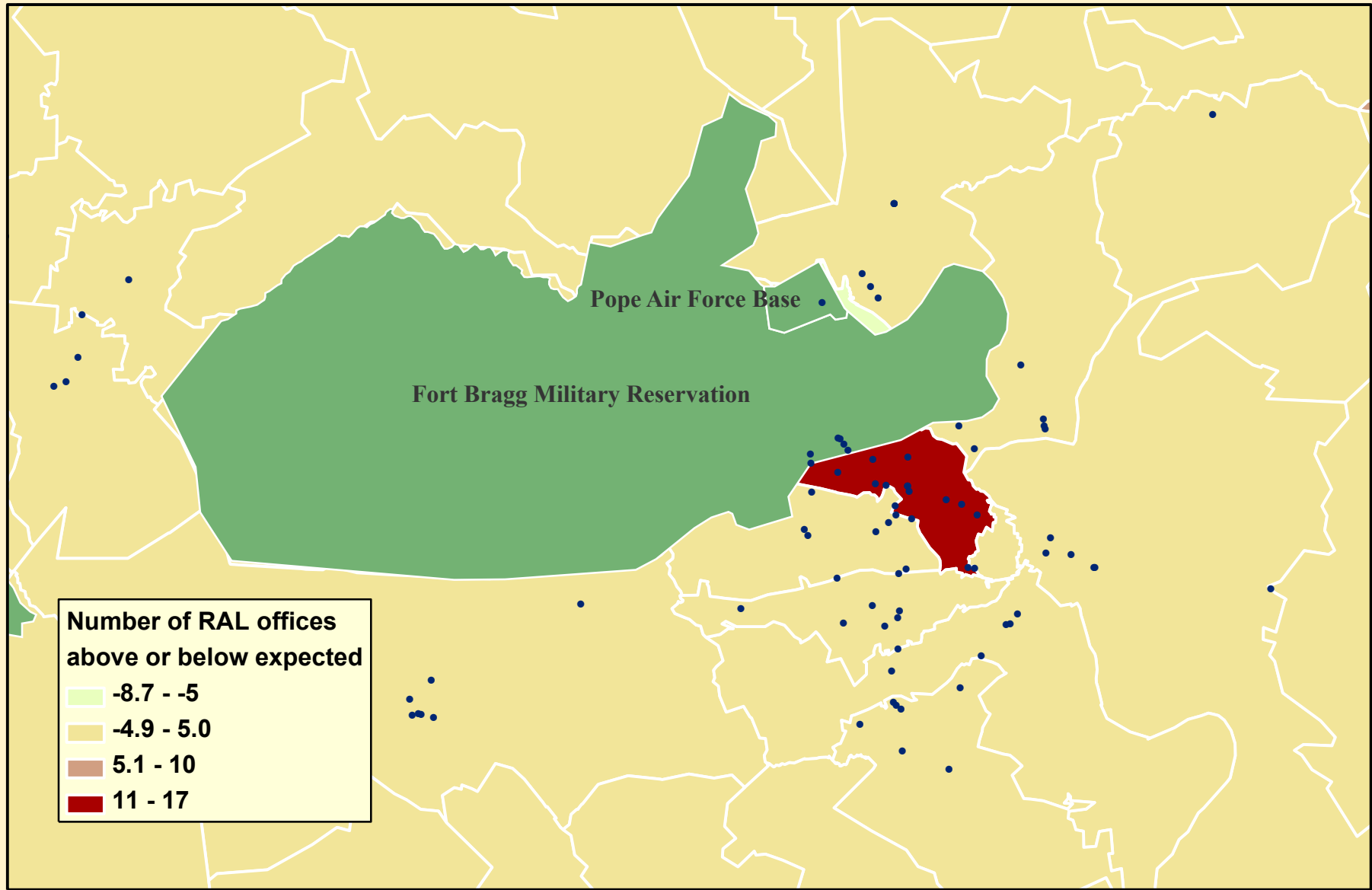
# Refund Anticipation Loan Offices by ZIP Code North Carolina

Steven M. Graves, PhD.  
Department of Geography  
California State University, Northridge



Source:  
North Carolina Commissioner of Banks  
Jan. 23, 2007





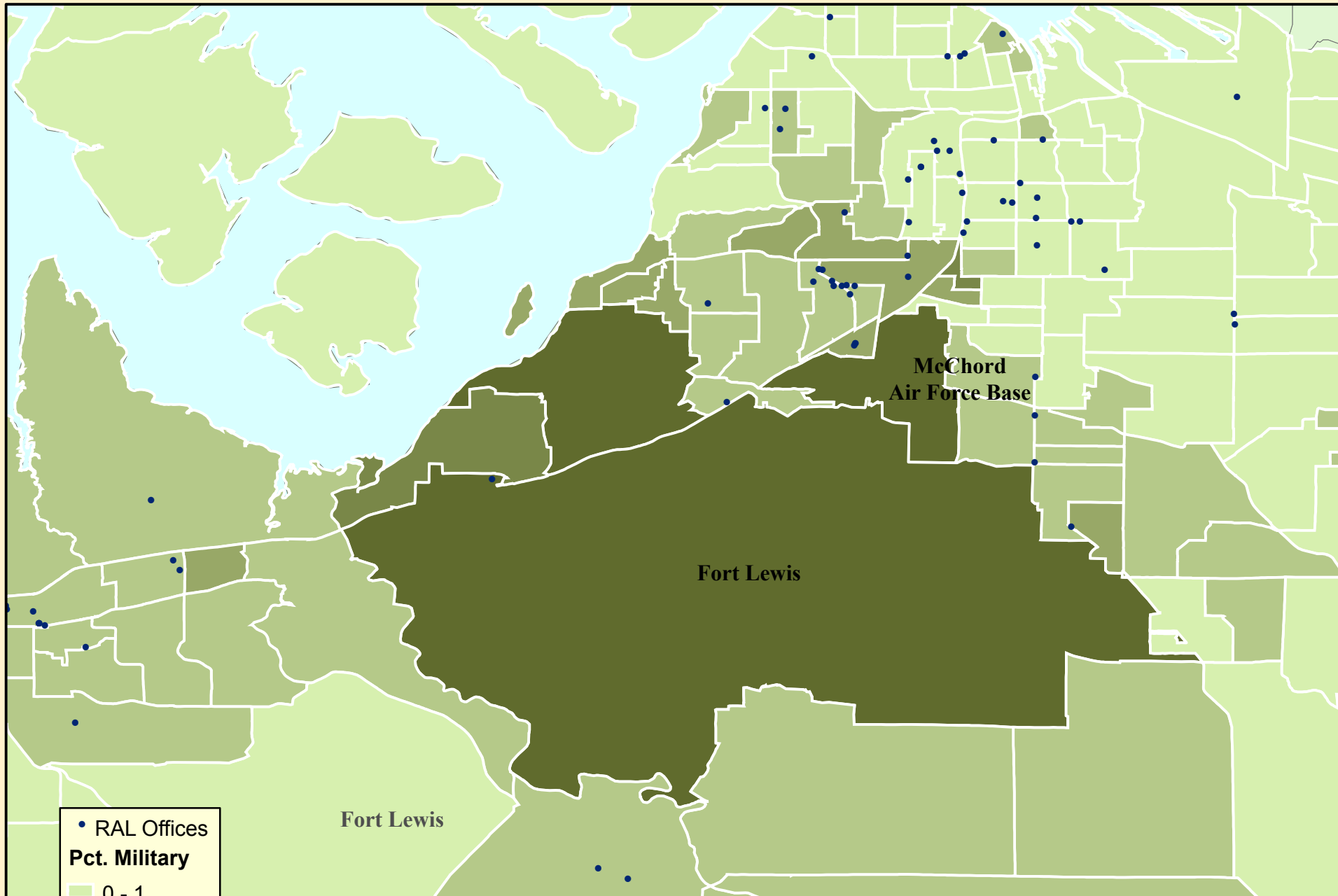
## Refund Anticipation Loan Offices by ZIP Code Fort Bragg/Pope AFB Region

Steven M. Graves, PhD.  
Department of Geography  
California State University, Northridge

0 0.306 1.2 1.8  
Miles

Source:  
North Carolina Commissioner of Banks  
Jan. 23, 2007





- RAL Offices

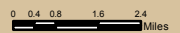
**Pct. Military**

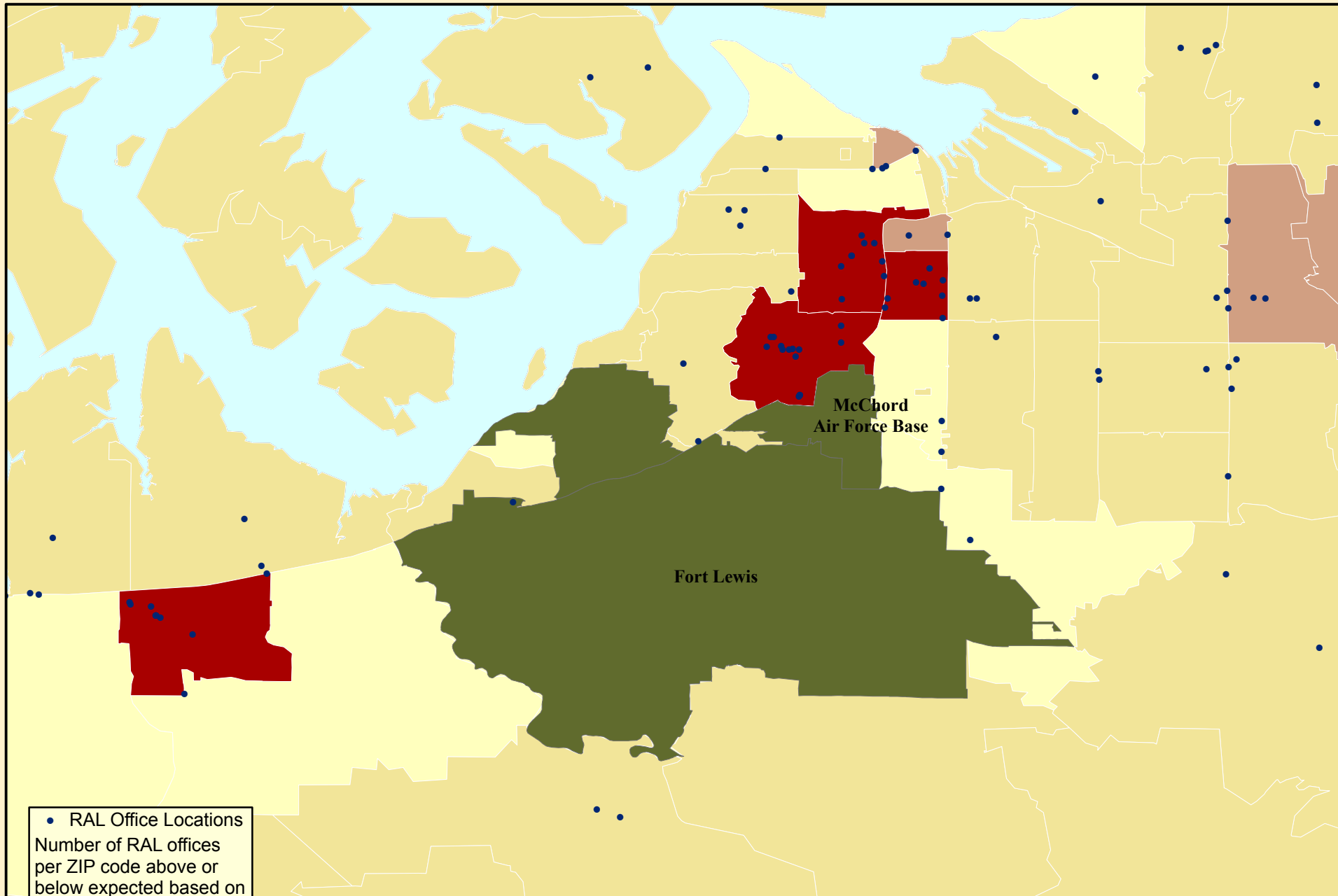
- 0 - 1
- 2 - 5
- 6 - 10
- 11 - 25
- 26 - 66

# Refund Anticipation Loan Offices Fort Lewis and McChord AFB Region

Dr. Steven Graves  
Department of Geography  
California State University, Northridge  
January, 2007

Sources: State of Washington  
Department of Financial Institutions

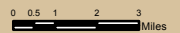




- RAL Office Locations
- Number of RAL offices per ZIP code above or below expected based on population
- 4.1 - -1
- 0.90 - 1.0
- 1.1 - 5.0
- 5.1 - 11

# Refund Anticipation Loan Offices Fort Lewis and McChord AFB Region

Dr. Steven Graves  
 Department of Geography  
 California State University, Northridge  
 January, 2007



Sources: State of Washington  
 Department of Financial Institutions

