

Refund loans tax poorest of filers

Taxpayers in 14621 neighborhood paid \$3.5M in fees for fast cash, study says

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Rather than wait a few weeks to get their tax refunds from the IRS, taxpayers in Rochester's lowest-income neighborhoods are shelling out millions of dollars in fees to tax preparers who offer quickie loans against the refunds at exorbitant annual percentage rates.

Taxpayers in the 14621 ZIP code — one of the poorest in the city — were among the hardest hit in the state, paying nearly \$3.5 million in fees for the loans, according to the Neighborhood Economic Development Advocacy Project, which analyzed four years of IRS data. Taxpayers in 14610, which includes the comparatively well-off Browncroft neighborhood, paid \$236,610 over the same period, while those in a Pittsford ZIP code paid \$140,120.

What's at stake

The financial well-being of some of our poorer citizens. Refund anticipation loans are financial products provided by third-party banks that are available through tax preparation offices. While tax preparers maintain that the product is useful and appropriately marketed, consumer advocates contend it is a form of predatory lending that siphons money from low-income neighborhoods.

All told, "tax refund anticipation loans," or RALs, cost Monroe County taxpayers more than \$29 million between 2002 and 2005, the neighborhood project found.

The group, based in New York City, contends that RALs are in essence high-cost loans — with annual percentage rates of 36 percent to 500 percent — marketed to low-income taxpayers as a way to obtain fast cash.

The loans are marketed by commercial tax preparers, such as Jackson Hewitt and H&R Block, and their partner banks. Even some used car dealers offer RALs for down payment use.

Melissa Horton, 41, of Rochester, had "always used H&R Block," for tax preparation and would take out a RAL to pay outstanding holiday bills and buy birthday presents for her mother and sister.

"I usually came out spending almost four hundred dollars just to get that done," said Horton, referring to the cost of both having her taxes done and the RAL fees. "As I got a little bit older, I realized it wasn't necessary."

Setting limits

How the loans work: The tax preparer sets up a temporary account for the borrower at a partner bank. After the IRS deposits the refund into the account, the bank deducts service and loan fees, and then issues the difference to the tax preparer. Borrowers typically pay three fees, according to information from the National Consumer Law Center and Consumer Federation of America: a federal and state tax form preparation fee; an electronic filing fee; and a finance charge assessed on a sliding scale based on the expected refund.

Interest rates for RALs are not subject to state usury caps — in New York it's 25 percent — because the banks that offer the advances are federally regulated.

Chris Keeley of the neighborhood project said the U.S. Office of the Comptroller has claimed that holding banks accountable to individual states' usury caps would be onerous, because their products are available nationwide. To avoid that problem, he said, the comptroller's office should set a national standard.

Meanwhile, "it's the Wild, Wild West. Anybody can throw up a sign, and anybody can act as a loan broker in these situations," said Keeley, whose organization has pressed for legislation that would require lenders to register with the state and ensure loans are in borrowers' best interests.

U.S. Sen. Charles Schumer, D-N.Y., who sits on the U.S. Senate Banking committee, has taken up the fight, as well, introducing legislation that would place limitations on RALs and the IRS' participation in the practice. (The IRS shares private tax return information with tax preparers, which can then be used to market various products.)

Fast cash

Despite what may seem like obvious pitfalls, RALs are popular with some consumers because they provide rapid access to cash for purchases. But for millions of low-income families, one credit union warns, RALs are quick money to pay for food and shelter, and even the cost of preparing their tax forms.

These are the people to whom RALs are marketed, in ubiquitous television advertisements and billboards — the population who can least afford it, Keeley said. According to a 2004 report, recipients of the Earned Income Tax Credit, a federal program that provides lump-sum benefits to working poor families through the tax system, made up 55 percent of RAL borrowers.

RALs are just one of an assortment of fast-cash products available today. Increasingly popular are "pay stub" and "holiday" loans, which are made before tax season begins, and are based on a projection of the borrower's tax refund and tax credits using the person's pay stub.

Representatives for the industry say they are fulfilling a need, particularly for people who don't have a bank account and therefore can't have their refunds deposited directly by the IRS. Representatives for both H&R Block and Jackson Hewitt said their clients were fully informed of the loan costs.

At Jackson Hewitt, "RAL applicants are provided with a variety of both verbal and written disclosures and information, before and during the tax preparation interview, such as: a product options grid ...; an office desk mat that provides the customer with an easy to understand comparison of the various products and services available; a refund anticipation loan ("RAL") Wall Poster that provides the customer with additional information on RALs ... (and) written documents," Sheila Cort, the company's corporate communications vice president, said in an e-mailed statement.

At H&R Block, customers go through "a five-part disclosure process," said spokesman Dan Smith, during which they are informed first of no-cost options such as e-filing. They also are told of a potential waiting period of eight to 15 days — "an internal number" based on information from the IRS Web site, Smith said — that it can take to get their refunds from the IRS. RALs, they are told, take one to two days. Or, they can opt for instant money, sometimes just a portion of the total they would receive from their refunds, for an additional fee.

"We absolutely educate our clients about those options, and we encourage our clients to explore no-cost delivery options. But for those for whom eight to 15 days is unacceptable, there is an option," Smith said. In 2006, he said, 4 million of H&R Block's 19.5 million clients used a refund anticipation loan. H&R Block's fees, he said, "are 85 percent less than a payday loan, 45 percent cheaper than a credit card cash advance and a fraction of the cost of our competitors."

Adding up the fees

Keeley, who pointed out that payday loans are illegal in New York, said: "Just because they're cheaper doesn't make them a responsible product."

"We agree there is a demand for short-term loans, but because there's a demand doesn't mean these products should be taking advantage of people," he said. "These loans are very specifically targeted to these people at the one time of year they have money coming back to them."

The money an individual parts with for a RAL — on average \$250, according to the consumer law center — isn't of as much concern to advocates as the cumulative effect of the fees. Over time, they say, they add up to millions, drained from places most in need of the resources.

"Think, if we had pooled that money differently, what we could have done in the neighborhood," said Joan Roby-Davison, executive director of Group 14621. "I can understand why people do the RALs. They have emergencies. They've got bills that are urgent. But in some cases they might not know there are other options, or how fast you can get (a refund) these days. I'm not sure people are aware that a little patience will actually put more money in their pockets. To see that much money just leave the neighborhood and not come back in any meaningful manner ... it's pretty appalling."

This year, Melissa Horton went to a free tax-preparation site run by the C.A.S.H. coalition, a group of 30 organizations led by the United Way of Greater Rochester that are working to help households eligible for Earned Income Tax Credits make the most of their money. Last year, C.A.S.H. prepared about 10,400 returns, said director Rita Eygabroad.

"I did the e-filing — the refund comes back in ten days, which is just as good — and also I got a lot of information, plus I got a little more money than I would have gotten going back to H&R Block," said Horton, who works in collections at Strong Memorial Hospital.

More consumers need to be educated, said Ruhi Maker, a lawyer with the Empire Justice Center. "If you've got RG&E shut off, or your landlord is at your door, maybe you're going to do it anyway," she said.

Of 600 people who last year expressed an interest in RALs when they had their taxes prepared through C.A.S.H., she said, only six took them after learning more.

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