

MODEL REFUND ANTICIPATION LOAN ACT

National Consumer Law Center

Introduction

Refund anticipation loans (RALs) are short term, high cost loans secured by and repaid from the proceeds of a consumer's tax refund from the Internal Revenue Service (IRS). Instead of waiting to receive tax refunds, RAL customers borrow against part or all of their expected tax refund. Consumers pay several fees to get a RAL: a loan fee for the RAL, an "administrative" or "electronic filing" fee, and a fee to a commercial tax preparer for filling out the federal and state tax forms.¹ In 2004, typical loan fees ranged from \$35 to \$105. Administrative fees can range from \$30 to \$55, and tax preparation fees average around \$120. What the consumer receives in hand is the refund minus the loan fee, the administrative fee, and the tax preparation fee. For the average refund of about \$2,100, the total amount of the three fees might be around \$250.²

RALs speed up receipt of cash from tax refunds, but not by much. A RAL puts cash into the consumer's hand in one or two days, or even on the same day for an extra fee, accounting for its appeal. However, the IRS has stated that a consumer who uses electronic filing and has a bank account into which the refund can be direct deposited can receive a refund in as little as 10 days.³

RALs Are High Cost

RALs carry triple digit Annual Percentage Rates (APRs) based on this 10 day period. Typical RAL loan fees translate into APRs of about 70% to over 700%. However, some tax preparers and RAL lenders have been reporting lower APRs by "unbundling" charges in order to make the loans look less expensive.⁴

Mechanics of RALs

RALs are usually not made by the tax preparer, but by a separate lender, usually a bank. Tax preparers facilitate the loans in partnership with the banks. The advantage of these partnerships is the ability of the bank to charge the rate allowed by its home state due to the doctrine of rate exportation.⁵ Another reason for these partnerships is that IRS rules do not permit tax preparers to act as RAL lenders.⁶

¹ 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, at 5. [hereinafter "NCLC/CFA 2002 RAL Report"], available at http://www.consumerlaw.org/initiatives/refund_anticipation.

² 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" National Consumer Law Center and Consumer Federation of America, January 29, 2004. [hereinafter "NCLC/CFA 2004 RAL Report"], at 5, available at http://www.consumerlaw.org/initiatives/refund_anticipation.

³ NCLC/CFA 2002 RAL Report at 5-6.

⁴ NCLC/CFA 2004 RAL Report at 5.

⁵ NCLC/CFA 2002 RAL Report at 18-19.

⁶ IRS Publication 1345.

RALs work like this:⁷ When the loan is made, the bank prepares to collect on the loan by opening a temporary or “dummy” bank account for the borrower to receive electronic deposit of the refund. The documents signed by the borrower instruct the IRS to direct deposit the refund into that account. The contract usually contains a right of set-off, which means that the creditor can take the money directly out of the dummy account without the consumer’s authorization. Thus, the creditor is repaid when the refund appears in the dummy account.⁸

Consumer Confusion Over RALs

Some consumers are misled into thinking of RALs as “quick refunds,” not understanding that they are loans. Consumers also sometimes do not understand that they are liable for the full amount of the loan if they do not receive all or part of their refund from the IRS. The refund amount would be affected if, for example, the IRS disallows a deduction or if there is an intercept of the refund for child support, student loan, or other debt.⁹

Drain on the Working Poor

RALs drain billions from the pockets of consumers and the U.S. Treasury. They are targeted at the working poor who receive the Earned Income Tax Credit (EITC). Approximately 12.7 million consumers paid about \$1.5 billion in RAL and associated fees in 2002. Over 50% of these RAL consumers, or 7 million, were working poor families who receive the EITC.

Current Regulation of RALs

The IRS has a handful of regulations governing RALs.¹⁰ They required tax preparers to disclose that a RAL is an interest bearing loan, a RAL is not a substitute for or faster way to receive a refund; and if the refund is not received by the RAL lender within the expected time frame, the taxpayer may be liable for additional interest on the RAL. The IRS regulations prohibit the tax preparer from receiving a fee for a RAL unless it is a flat fee.¹¹

⁷ NCLC/CFA 2002 RAL Report at 6.

⁸ There is also a non-loan product related to RALs called a refund anticipation check (RAC). With a RAC, the bank opens the temporary or “dummy” bank account, then waits for the IRS to direct deposit the consumer’s refund. After the refund is received, 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. Because there is no loan, RACs take about the same amount of time as if the consumer electronically filed and had the IRS direct deposit the refund into the consumer’s own bank account. RACs are used as the default product if the consumer is denied a RAL. RACs generally cost about \$25 to \$28. NCLC/CFA 2003 RAL Report at 6-7.

⁹ NCLC/CFA 2002 RAL Report at 6.

¹⁰ The IRS rules are set forth in IRS Publication 1345, an IRS document that governs providers of electronic tax return filing or “e-file providers”. E-file providers include tax preparers who engage in the electronic filing of returns. The vast majority of tax preparers who facilitate RALS are e-file providers.

¹¹ IRS Publication 1345. A more detailed summary of these IRS regulations is available in the NCLC/CFA 2002 RAL Report at 17-18.

As of early 2004, there were 4 states¹² and one municipality with laws regulating RALs.¹³ Most of these laws focus on the tax preparers who facilitate RALs, and require disclosures about the nature, costs and risks of RALs.¹⁴ North Carolina has the most comprehensive RAL statute, requiring disclosures, postings, and registration of RAL facilitators.¹⁵ It also authorizes the Commissioner of Banks to find that a RAL loan fee is unconscionable and prohibits facilitators from charging such a fee. The Model RAL Act uses the North Carolina RAL statute as a template, then adds a number of important protections.

Goals of the Model RAL Act

This Model Act is designed to reduce some of the most serious problems associated with RALs. It is a state statute primarily targeted at the facilitators of RALs and refund anticipation checks (RACs). While some of the provisions will apply to creditors, the doctrine of rate exportation discussed above makes it more effective and important to regulate the tax preparers who act as loan brokers for RALs.

Summary of Provisions

The Model Act includes provisions to limit RAL fees, prohibit debt collection abuses by facilitators, and prevent referrals to check cashers. It provides for mandatory disclosures in both wall postings and a disclosure sheet accompanying the RAL application. In addition, the Model Act contains registration and bonding requirements designed to ensure state oversight and assure compliance with the Act. Importantly, the Model Act grants consumers a private right of action to recover damages, costs and attorneys fees.

The Model Act can be enacted on a stand alone basis, or it can also be enacted as part of a comprehensive set of regulations governing tax preparers. Most states and the federal government have very little regulation of tax preparers.¹⁶

The consumer protections included in the Model RAL Act can benefit the growing numbers of consumers who are sold RALs, especially working poor Americans who receive the EITC. These protections will benefit not only consumers, but also the U.S. Treasury, which pays out the EITC benefits that are drained by RALs every year.

¹² Ill. Comp. Stat. Ann. ch. 815, § 177/1, *et seq.*; Minn. Stat. § 270.30; N.C. Gen. Stat. §§ 53-245 to 53-254; and Wis. Stat. §§ 421.301 and 422.310.

¹³ New York City Administrative Code, Section 20-739, *et seq.*

¹⁴ For a summary of some of these laws, *see* NCLC/CFA 2004 RAL Report at 13-14.

¹⁵ N.C. Gen. Stat. §§ 53-245 to 53-254.

¹⁶ NCLC/CFA 2002 RAL Report at 17

MODEL REFUND ANTICIPATION LOAN ACT

with Commentary
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Section 1. Title and scope.

(a) Title. This Act shall be known and cited as the "Refund Anticipation Loan Act". This Act shall be liberally construed to effectuate its purpose. The purpose of the Act is to protect consumers who enter into refund anticipation loan and refund anticipation check transactions and to limit fees for refund anticipation loans facilitated in this state. This Act is to be construed as a consumer protection statute for all purposes.

(b) Scope. No person (including any officer, agent, employee or representative) may individually or in conjunction or cooperation with another person: (a) solicit the execution of, process, receive, or accept an application or agreement for a refund anticipation loan or refund anticipation check, or (b) in any other manner facilitate the making of a refund anticipation loan or refund anticipation check unless the person has complied with the provisions of this Act. The provisions of this Act shall apply to any person who seeks to evade its applicability by any device, subterfuge, or pretense whatsoever.

Commentary

Subsection (a) sets the stage for the remainder of the Act by clearly announcing that the legislature intends that: the Act must be liberally construed to effectuate its purpose; it enunciates a specific purpose; and it is a consumer protection law. Subsection (b) defines a broad scope of coverage for the Act, and makes clear that the scope includes those who attempt to evade the Act. These directives will give guidance to the courts when the Act's provisions are applied and interpreted.

Section 2. Definitions.

The following definitions apply in this Act:

(a) Applicant shall mean a person who applies for registration as a facilitator of refund anticipation loans or refund anticipation checks.

(b) Commission shall mean the State _____ Commission.

(c) Commissioner shall mean the Commissioner of _____.

(d) Consumer shall mean any natural person who, singly or jointly with another consumer, is solicited for, applies for, or receives the proceeds of a refund anticipation loan or refund anticipation check.

(e) Creditor shall mean any person who makes a refund anticipation loan or who takes an assignment of a refund anticipation loan.

(f) Facilitator shall mean a person who individually or in conjunction or cooperation with another person: (i) solicits the execution of, processes, receives, or accepts an application or agreement for a refund anticipation loan or refund anticipation check, or (ii) in any other manner facilitates the making of a refund anticipation loan or refund anticipation check.

(g) Person shall mean an individual, a firm, a partnership, an association, a corporation, or another entity.

(h) Refund anticipation check shall mean a check or other payment mechanism: (i) representing the proceeds of the consumer's tax refund; (ii) which was issued by a depository institution or other person that received a direct deposit of the consumer's tax refund or tax credits; and (iii) for which the consumer has paid a fee or other consideration for such payment mechanism.

(i) Refund anticipation loan shall mean a loan that is secured by or that the creditor arranges to be repaid directly or indirectly from the proceeds of the consumer's income tax refund or tax credits. A refund anticipation loan also includes any sale, assignment, or purchase of a consumer's tax refund at a discount or for a fee, whether or not the consumer is required to repay the buyer or assignee if the Internal Revenue Service denies or reduces the consumer's tax refund.

(j) Refund anticipation loan fee shall mean the charges, fees, or other consideration charged or imposed directly or indirectly by the creditor or facilitator for the making of or in connection with a refund anticipation loan. This term includes any charge, fee, or other consideration for a deposit account, if the deposit account is used for receipt of the consumer's tax refund to repay the amount owed on the loan. This term does not include any charge, fee, or other consideration usually charged or imposed by the facilitator in the ordinary course of business, such as fees for tax return preparation and fees for electronic filing of tax returns, if the same fees in the same amount are charged to the facilitator's customers who do not receive refund anticipation loans or refund anticipation checks.

(k) Refund anticipation loan interest rate shall mean the interest rate for a refund anticipation loan calculated as follows: the total amount of refund anticipation loan fees divided by the loan amount (minus any loan fees), then divided by the number of days in the loan term, then multiplied by 365 and expressed as a percentage. The total amount of the refund anticipation loan fee used in this calculation shall include all refund anticipation loan fees as defined in subsection (j). If a deposit account is established or maintained in whole or in part for the purpose of receiving the consumer's tax refund to repay the amount owed on a refund anticipation loan:

(i) the maturity of the loan for the purpose of determining the refund anticipation loan interest rate shall be assumed to be the estimated date when the tax refund will be deposited in the deposit account; and

(ii) any fee charged to the consumer for such deposit account shall be considered a loan fee and shall be included in the calculation of the refund anticipation loan interest rate.

If no deposit account is established or maintained for the repayment of the loan, the maturity of the loan shall be assumed to be the estimated date when the tax refund is received by the creditor.

(l) Registrant shall mean a person who is registered as a facilitator of refund anticipation loans or refund anticipation checks under this Act.

Commentary

There are a number of critical definitions in the Act:

(b) *“Commission” is the state agency charged with the responsibility of enforcing the Act.*

(c) *“Commissioner” is the head of the state agency defined in (b).*

(e) *“Creditor” includes both the entity that makes a RAL as well as any assignees.*

(f) *“Facilitator” is defined broadly to include any person who solicits for, processes, receives or accepts a RAL or RAC application, or otherwise facilitates a RAL or RAC. It is meant to cover tax preparers and any other entities that broker RALs or RACs. This definition is similar to the definition of “facilitator” in the North Carolina RAL statute, N.C. Gen. Stat. § 53-246(6).*

The concept of the RAL facilitator is the most critical concept in the Model Act. States are limited in their ability to regulate the banks that make RALs due to preemption by federal banking statutes and regulators. In particular, the doctrine of rate exportation preempts state usury laws by allowing banks to charge the maximum interest rate permitted in the banks’ own home states – to avoid usury caps, banks simply charter in a state without one. The Model Act deals with the limitations of state regulatory power by having the concept of a “facilitator” and regulating that facilitator. To regulate RAL interest rates, the Model Act prohibits the facilitation of a usurious loan. Thus, even if making a loan with triple digit interest rates is permissible because of federal preemption, facilitation of that loan will be illegal.

Some RALs are not made through tax preparers by banks, but directly by the creditor (such as the storefront lender in the case of State ex rel. Salazer v. The Cash Now Store, 31 P.3d 161 (Colo. 2001)). In these cases, the creditor will also be the “facilitator” because it solicits and accepts the RAL application directly. The following language may be added to the definition of “facilitator” to reinforce this point: “If there is no third party facilitator because a creditor directly solicits the execution of, receives, or accepts an application or agreement for a refund anticipation loan or refund anticipation check, that creditor shall be considered a facilitator.”

(h) *“Refund anticipation check” includes the non-loan bank product that many RAL creditors and tax preparers offer in addition to RALs. With refund anticipation checks (RACs), 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. It is important to regulate RACs because they are closely related to RALs, and*

are used as the default product if the consumer is denied a RAL. Furthermore, RACs carry their own fees, which consumers could avoid by having their refunds direct deposited into their own bank accounts. Consumers without bank accounts should be encouraged to open permanent bank accounts instead of paying significant fees for a temporary account.

(i) “Refund anticipation loan” is defined broadly and includes loans in which either the loan is secured by a tax refund or the creditor arranges for the loan to be repaid from a tax refund or tax credits. The definition also includes those loans made by non-bank entities that are styled as an assignment or a “chase in action,” such as the loan at issue in the case of State ex rel. Salazer v. The Cash Now Store, 31 P.3d 161 (Colo. 2001).

(j) “Refund anticipation loan fee” is defined to include any fees that are associated with the making of a RAL. The definition specifically includes any fee for a temporary or “dummy” bank account used to receive a direct deposit of the consumer’s tax refund to repay the RAL. Many RAL lenders have disaggregated or “unbundled” an amount they denominate to be a fee for this dummy bank account, making the finance charge and Annual Percentage Rate (APR) under the federal Truth-in-Lending Act (TILA) look lower. However, inclusion of this amount in the RAL fee will give a more accurate picture of the true costs of a RAL. Similarly, RAL lenders and tax preparers have “unbundled” other fees by imposing them on RAC customers, such as administrative fees. RAL lenders presumably rely on an argument that these fees are not RAL finance charges under the TILA definition because they are the same as those imposed in “comparable cash transactions,” i.e., RACs. As a result, many RAL lenders disclose deceptively low APRs for what is really a very high-cost short-term loan. Thus, the definition of a RAL fee excludes tax preparation, electronic filing, and other fees only when these fees are also charged to customers who do not receive either a RAL or a RAC. It is critical that the scope of this exclusion remain narrow.

(k) “Refund anticipation loan interest rate” is the annualized rate for a RAL that includes all RAL fees defined in (j) above, including the dummy account fee. The RAL interest rate may differ from the APR disclosed by RAL creditors under TILA, if the creditors exclude various fees (such as the dummy account fee) from the TILA finance charge and APR calculation. The legality of such exclusions is arguable under TILA. This Act avoids the necessity to resolve this issue under TILA by mandating a separate and different annualized interest rate disclosure, using a term other than “APR”, to reflect the true cost of credit for a RAL.

The definition of the RAL interest rate provides for a formula to calculate the rate. The definition requires that the RAL interest rate be based upon the estimated time period for when the consumer’s tax refund is direct deposited into the dummy account. The following is an example of how this formula works.

Formula: RAL fees divided by loan amount, divided by days in loan term, then multiplied by 365 and expressed as a percentage.

Example:

Amount of refund - \$2,000

Total amount of RAL fees - \$15

Loan amount - \$2,000 minus \$15 = \$1,985

Days in loan term (based on estimated receipt of consumer's tax refund into dummy account) – 10 days

\$15 (total RAL fees) divided by \$1,985 (loan amount) = 0.0076

Divided by 10 (days in loan term) = 0.00076

Multiplied by 365 = 0.2774

Multiplied by 100 (to express as a percentage) = 27.74%

Section 3. Registration and bond requirement.

(a) Registration Requirement. No person may individually or in conjunction or cooperation with another person solicit the execution of, process, receive, or accept an application or agreement for a refund anticipation loan or refund anticipation check without first being registered with the Commissioner and posting a bond in accordance with the procedures provided in this Act.

(b) Bond. Each facilitator must post a bond in the amount of \$100,000 per location, which must continue in effect for 5 years after the facilitator ceases operation in the state. Such bond must be available to pay damages and penalties to consumers harmed by any violation of this Act.

(c) Exemption. This section does not apply to a person doing business as a bank, thrift, savings association, or credit union, under the laws of the United States or of this state.

Commentary

This section ensures that any entity which facilitates RALs is registered with a state agency so that there is regulatory oversight of facilitators. The registration requirement is similar to the requirement in the North Carolina RAL statute, N.C. Gen. Stat. § 53-247. This section also mandates that facilitators post a bond in the amount of \$100,000 that can be used to pay damages and penalties to consumers harmed by any violations of the Act. Only one bond is required per location. The bond is important because it provides a source of compensation to harmed consumers. Without this protection, these businesses could sell, transfer, or skim off their assets and leave nothing from which a consumer could satisfy a judgment obtained due to the illegal acts of a company.

Section 4. Registration procedure; informal hearing.

(a) Initial Registration. An application to become registered as a facilitator shall be in writing, under oath, and in a form prescribed by the Commissioner. The application shall contain all information prescribed by the Commissioner. Each application for registration shall be accompanied by a fee, payable to the Commissioner, of _____ (\$____) for each office where the registrant intends to facilitate refund anticipation loans or refund anticipation checks.

Upon the filing of an application for registration, if the Commissioner finds that the responsibility and general fitness of the applicant are such as to command the confidence of the community and to warrant belief that the business of facilitating refund anticipation loans or refund anticipation checks will be operated within the purposes of this Act, the Commissioner shall register the applicant and shall issue and transmit to the applicant a certificate attesting to the registration. If the Commissioner does not so find, he shall not register the applicant and shall notify the applicant of the reasons for the denial.

Upon receipt of a certificate of registration, the applicant is registered under this Act and may engage in the business of facilitating refund anticipation loans and refund anticipation checks at the offices identified on the application for registration.

(b) Renewal. Each registration as a facilitator of refund anticipation loans and refund anticipation checks shall expire on December 31 following the date it was issued, unless it is renewed for the succeeding year. Before the registration expires, the registrant may renew the registration by filing with the Commissioner an application for renewal in the form and containing all information prescribed by the Commissioner. Each application for renewal of registration shall be accompanied by a fee of _____dollars (\$____) for each office where the registrant intends to facilitate refund anticipation loans or refund anticipation checks during the succeeding year.

Upon the filing of an application for renewal of registration under this Act, the Commissioner shall renew the registration, provided that no registration shall issue if the Commissioner finds that the registrant has violated this Act or determines that the fitness of the registrant or the operations of the registrant would not support registration of the registrant under subsection (a). If the Commissioner makes such a finding or determination, he shall so notify the registrant, stating the reasons for the determination.

(c) Display of Certificate. Each registrant shall prominently display a certificate issued under this Act in each place of business in the State where the registrant facilitates the making of refund anticipation loans or refund anticipation checks.

(d) Within five days of receipt of the Commissioner's notice, as required by subsections (a) and (b) of this section, the applicant may make written demand of the Commissioner for a hearing. The hearing before the Commissioner shall be an informal hearing and shall be held with reasonable promptness.

Commentary

The Act puts the burden on the Commissioner to make certain findings in order to register a RAL/RAC facilitator or to renew a registration. The most critical finding is for registration renewals, whether the registrant has violated the provisions of this Act. This finding ensures that facilitators who violate the Act are prevented from continuing to facilitate RALs and RACs. The Act also requires the Commissioner to find that the applicant's characteristics are sufficient to "command the confidence of the community" and to warrant belief that the applicant will abide by the provisions of the Act. These findings are intended to screen out questionable businesses that engaged in RAL/RAC facilitation, as well as tax preparation.

The registration procedures in this section are similar to those in the North Carolina RAL statute, N.C. Gen. Stat. § 53-248. A comprehensive licensing scheme for tax preparers could take the place of these registration requirements. However, any such scheme should include a provision that a registration cannot be renewed if the registrant has violated the provisions of the Act governing RALs and RACs.

Section 5. Posting of Fee Schedule and Disclosures

(a) Every facilitator shall display a schedule showing the current fees for refund anticipation loans facilitated at the office, for refund anticipation checks facilitated at the office, and for the electronic filing of the consumer's tax return.

(b) Every facilitator shall display on each fee schedule examples of the refund anticipation loan interest rates for refund anticipation loans of two hundred dollars (\$200.00), five hundred dollars (\$500.00), one thousand dollars (\$1,000), one thousand five hundred dollars (\$1,500), two thousand dollars (\$2,000), and five thousand dollars (\$5,000). The refund anticipation loan interest rate shall be calculated as set forth in section 2(k) of this Act.

(c) Every facilitator shall also prominently display on each fee schedule: (i) a legend, centered, in bold, capital letters, and in one-inch letters stating: NOTICE CONCERNING REFUND ANTICIPATION LOANS; and (ii) the following verbatim statement: "When you take out a refund anticipation loan, you are borrowing money against your tax refund. If your tax refund is less than expected, you must still repay the entire amount of the loan. If your refund is delayed, you may have to pay additional costs. YOU CAN GET YOUR REFUND IN ABOUT 10 DAYS WITHOUT GETTING A LOAN. You can have your tax return filed electronically and your refund direct deposited into your own bank account without obtaining a loan or paying fees for an extra product."

(d) The postings required by this section shall be made in no less than 28-point type on a document measuring no less than 16 inches by 20 inches. The postings required in this section shall be displayed in a prominent location at each office where the facilitator is facilitating refund anticipation loans.

(e) No facilitator may facilitate a refund anticipation loan or refund anticipation check unless (i) the disclosures required by this section are displayed; (ii) the fee actually charged for the refund anticipation loan or refund anticipation check is the same as the fee displayed on the schedule; and (iii) for refund anticipation loans, the refund anticipation loan interest rate does not exceed [36% per annum or the rate set forth in other applicable state law, if any, whichever is lower]. The refund anticipation loan interest rate shall be calculated as set forth in section 2(k) of this Act.

Commentary

The Act requires postings so that consumers who enter a facilitator's office immediately know the nature, costs, and risks of RALs. Having postings in addition to application disclosures are important because, in some instances, consumers may not be given sufficient opportunity or time to review application disclosures. Postings will catch a consumer's eye and ensure that critical information is brought to the consumer's attention. The Act has mandatory size and font requirements to ensure that the disclosures are of a sufficiently large size to be prominent and legible. The North Carolina RAL statute similarly has posting requirements but does not use mandatory language. N.C. Gen. Stat. § 53-249.

The Act requires some of the posting disclosures to be made using mandatory language. A significant percentage of the taxpayers who get RALs and RACs, including EITC recipients, have limited educational and literacy skills. For example, an estimated 46 to 51% of the general population and 76% of food stamp recipients do not have adequate literacy skills to complete the multiple tax forms necessary to claim the EITC itself.¹⁷ These consumers are therefore unlikely to understand the dense, technical, and lengthy RAL agreements currently used by some RAL creditors and facilitators. The Act's mandatory language requirements are meant to ensure that information is conveyed in language that is understandable to most consumers.

The mandatory warnings advise consumers of the following:

- *That a RAL is a loan.*
- *If the consumer's tax refund is less than expected, the consumer is liable for the full amount of the loan and must repay any difference.*
- *If the consumer's refund is delayed from the IRS, additional costs (such as late fees or additional interest) may be charged.*
- *Consumers can get their tax refunds in about 10 days without paying extra, with electronic filing and direct deposit.*

To prevent misrepresentation, this section makes it unlawful to charge a RAL or RAC fee that is different from the fee disclosed on the postings. It also prohibits such a fee from exceeding the RAL interest rate cap of either 36% per annum or the state usury cap, whichever is lower. The RAL interest rate cap is the key provision for protecting consumers from the harms of RALs. This cap is set forth in a couple of provisions in the Act to reinforce its importance.

¹⁷ Michael O'Connor, *Tax Preparation Services for Low Income Filers*, 90 Tax Notes 231, January 8, 2001.

Section 6. **Application Disclosures.**

At the time a consumer applies for a refund anticipation loan or check, the facilitator or creditor shall disclose to the consumer on a form separate from the application in 14-point type, unless otherwise noted:

- (a) The fee for the refund anticipation loan or refund anticipation check.
- (b) The fee for electronic filing of a tax return.
- (c) The time within which the proceeds of the refund anticipation loan or check will be paid to the consumer if the loan or check is approved.
- (d) For refund anticipation loans, the following disclosures: (i) a legend, centered, in bold, capital letters, and in 18-point type stating: NOTICE; and (ii) the following verbatim statement: “This is a loan. This loan is borrowing money against your tax refund. If your tax refund is less than expected, you must still repay the entire amount of the loan. If your refund is delayed, you may have to pay additional costs. **YOU CAN GET YOUR REFUND IN ABOUT 10 DAYS WITHOUT GETTING THIS LOAN.** You can have your tax return filed electronically and your refund direct deposited into your own bank account without obtaining a loan or other paid product.”
- (e) For refund anticipation loans, disclosure of the refund anticipation loan interest rate. The refund anticipation loan interest rate shall be calculated as set forth in section 2(k) of this Act.

(f) For refund anticipation checks, the following disclosures: (i) a legend, centered, in bold, capital letters, and in 18-point type stating: NOTICE; and (ii) the following verbatim statement: “You are paying [amount of refund anticipation check fee] to get your refund check through [name of issuer of refund anticipation check]. **YOU CAN AVOID THIS FEE AND STILL RECEIVE YOUR REFUND IN ABOUT 10 DAYS BY HAVING THE IRS DIRECT DEPOSIT YOUR REFUND INTO YOUR OWN BANK ACCOUNT.** You can also wait for the IRS to mail you a check. If you do not have a bank account, you may wish to consider getting one.”

Commentary

This section describes the disclosures that must be given to consumers prior to entering into a RAL or RAC agreement. These disclosures must be made in a document that is separate from the RAL/RAC application or agreement, and must be made in 14 point type unless otherwise indicated. This type size requirement is intended to ensure that consumers will actually be able to read the disclosures. Currently, some RAL creditors and facilitators make disclosures in type sizes of 10 point or less, which are difficult to read (especially for older consumers). These disclosures are often embedded in lengthy, dense, and technical documents, and are not conspicuous to consumers. To demonstrate the impact of the type sizes, compare

14 point type

12 point type

10 point type

8 point type

The Minnesota RAL statute, Minn. Stat. § 270.30, and New York City RAL ordinance, N.Y.C. Admin. Code § 20-741.1, both similarly use 14 point type. They also both include mandatory warnings

The disclosures required by this section include:

- *The fee for the RAL or RAC.*
- *If an electronic filing fee is charged (and it is not already included in the RAL or RAC fee because it is also charged to non-RAL/RAC consumers), it must be separately disclosed.*
- *When the consumer can expect to receive the RAL or RAC check if approved.*
- *For RALs, the RAL loan interest rate as calculated in section 2(k) of the Act. This disclosure is in addition to (and may differ from) the disclosure of the Annual Percentage Rate under the federal Truth-in-Lending Act for the reasons discussed in the Commentary to section 2(k).*
- *For RALs, a mandatory warning very similar to the posting warning in section 5(c).*
- *For RACs, a mandatory warning that the consumer is paying an extra fee for the RAC to receive their tax refund check, and information on how to receive a refund without paying the RAC fee.*

Section 7. Requirements for Refund Anticipation Loans and Refund Anticipation Checks

Any person (including any officer, agent, employee or representative) who makes or facilitates a refund anticipation loan or refund anticipation check shall:

- (a) Arrange such loan or check, or inform the consumer that the application is rejected, promptly after the consumer applies for the loan or check.
- (b) Provide to the consumer, prior to consummation of the loan or check transaction in a form that can be kept by the consumer: (i) a copy of the completed loan or check application and agreement; (ii) the disclosures required by section 6; and (iii) for refund anticipation loans, the disclosures required by the federal Truth-In-Lending Act.
- (c) Provide the disclosures required by section 6 in English and in the language in which the loan was negotiated.

Commentary

This section imposes several mandatory duties upon RAL/RAC facilitators and creditors. These include a duty to act promptly on a RAL or RAC application; a duty to give the consumer a

retainable copy of the loan application/agreement, the application disclosures in section 6, and the TILA disclosures; and a duty to provide the application disclosures in both English, and if the loan was negotiated in any other language, in the other language. The last duty is to ensure that limited English speakers are given the opportunity to read the application disclosures.

Section 8. Prohibited activities.

No person (including any officer, agent, employee or representative) in the making or facilitating of a refund anticipation loan or refund anticipation check shall:

(a) Engage in unfair or deceptive acts or practices in the facilitating of a refund anticipation check or in the making or facilitating of a refund anticipation loan, including misrepresenting a factor or condition of such loan or check or making any oral statements contradicting any of the information required to be disclosed under this Act.

(b) Fail to comply with any provision of this Act.

(c) Threaten to take any action that is prohibited by this Act or by any other law, or that the person does not actually intend to take.

(d) Make or facilitate a refund anticipation loan for which the refund anticipation loan interest rate is greater than [36% per annum or the rate set forth in other applicable state law, if any, whichever is lower]. The refund anticipation loan interest rate shall be calculated as set forth in section 2(k) of this Act. Any refund anticipation loan for which the refund anticipation loan interest rate exceeds [36% per annum or the rate set forth in other applicable state law, if any, whichever is lower] shall be void ab initio.

(e) Directly or indirectly charge, or arrange for the charging of, any interest, fee or charge related to a refund anticipation loan or refund anticipation check, other than those specifically authorized by this Act, including but not limited to: (i) charges for insurance; (ii) attorneys fees or other collection costs; or (iii) check cashing.

(f) Include any of the following provisions in any document provided or signed in connection with a refund anticipation loan or refund anticipation check, including the loan application or agreement:

(i) A hold harmless clause;

(ii) A confession of judgment clause;

(iii) A waiver of the right to a jury trial, if applicable, in any action brought by or against the consumer;

(iv) Any assignment of or order for payment of wages or other compensation for services;

(v) A provision in which the consumer agrees not to assert any claim or defense arising out of the contract, or to seek any remedies pursuant to section 10 of this Act;

(vi) A waiver of any provision of this Act. Any such waiver shall be deemed null, void and of no effect;

- (vii) A waiver of the right to injunctive, declaratory, other equitable relief, or relief on a class-wide basis; or
- (viii) A provision requiring that any aspect of a resolution of a dispute between the parties to the agreement be kept confidential. This provision shall not affect the right of the parties to agree that certain specified information is a trade secret or otherwise confidential or to later agree, after the dispute arises, to keep a resolution confidential.
- (g) Take or arrange for a creditor to take a security interest in any property of the consumer other than the proceeds of the consumer's tax refund to secure payment of a refund anticipation loan.
- (h) Directly or indirectly, individually or in conjunction or cooperation with another person, engage in the collection of an outstanding or delinquent refund anticipation loan for any creditor or assignee, including soliciting the execution of, processing, receiving, or accepting an application or agreement for a refund anticipation loan or refund anticipation check that contains a provision permitting the creditor to repay, by offset or other means, an outstanding or delinquent refund anticipation loan for that creditor or any creditor from the proceeds of the consumer's tax refund.
- (i) Facilitate, refer, or solicit consumers on behalf of a third party engaged in check cashing for a fee, or permit third party check cashing for a fee in any place of business identified on the application for registration.
- (j) Facilitate any loan that is secured by or that the creditor arranges to be repaid directly from the proceeds of the consumer's state tax refund from the State Treasury.
- (k) Make a misrepresentation of fact in obtaining or attempting to obtain a registration as a facilitator.
- (l) Engage in any other action prohibited by rules promulgated by the Commission.

Commentary

The list of prohibited acts in this section is crucial to protecting consumers from abusive behavior, and provides the real teeth of the Act. The most important prohibited act is subsection (d), which limits the RAL interest rate to no more than the applicable state usury cap or 36% per annum, whichever is lower (thus, if there is no state usury cap, the rate cap should be set at 36% per annum). The calculation of the RAL interest rate must be done according to the formula set forth in section 2(k).

The RAL interest rate cap is the crux of the consumer protections of the Act. It is designed to curb the exorbitant fees and charges that are currently the norm in the RAL industry while allowing RAL lenders a more than reasonable rate of return for a secured small loan. The 36% per annum rate cap is consistent with the rate limits for small, unsecured loans in states that have retained usury caps. Interest rates are understandably higher when a loan is unsecured. However, RALs are secured loans, and their risk is even lesser due to the direct deposit of the

refund and the fact that the IRS notifies tax preparers and lenders if the consumer's refund will be reduced because of a federal offset.¹⁸

The RAL interest rate cap applies to both creditors and facilitators. Because of federal preemption, the cap may not apply to RAL creditors that are banks. However, federal preemption for banks does not extend to the tax preparers that facilitate RALs. Thus, subsection (d) should be able to regulate RAL interest rates by prohibiting the facilitation of a loan in excess of the cap.

The protections of the interest rate cap at subsection (d) must be combined with subsection (e), which prohibits RAL facilitators from padding the cost of a RAL by adding fees for insurance, check cashing, or other services. Such fees are usually paid to third parties so as the escape inclusion in the loan fee, but then a portion is paid back to the lender or broker in the form of a "referral" fee or other kickback from the third party. By prohibiting such padding, subsection (e) ensures the effectiveness of the rate cap to limit RAL fees.

The next most important prohibited act is subsection (h), which prohibits RAL facilitators from engaging or assisting in debt collection for any RAL creditor. Almost all of the RAL creditors and facilitators engage in a particularly abusive debt collection practice involving set-offs from the dummy account. All of the RAL creditors have included a provision in their RAL and RAC agreements allowing them to take a consumer's tax refund and use it to pay back any prior RAL debts for any RAL lender. Thus, if a taxpayer owes money to one RAL lender from a prior year and applies for a RAL or RAC, the lender will seize her refund at the time it is deposited by the IRS into the dummy account, and use it to repay the prior RAL debt to itself or the other RAL lender. Very few consumers actually understand the risk of this type of debt collection when they apply for a RAL or RAC. Subsection (h) would prohibit this abusive practice.

Several other protections are critical, including the prohibitions against:

- *Unfair or deceptive acts or practices, including false threats.*
- *Inclusion of certain legal provisions in a RAL or RAC contract that are abusive toward consumers, such as a confession of judgment or a wage assignment clause.*
- *A RAL secured by a state tax refund.*
- *Violation of the Act or any regulations promulgated by the Commission under the Act.*

Section 9. Administrative remedies

(a) Cease and Desist Order. Whenever the Commission believes or has notice that any action of a facilitator may be in violation of this Act or the rules or regulations promulgated thereunder, or that the facilitator has engaged in an unfair or deceptive act or practice, the Commissioner shall give reasonable notice to the facilitator of the suspected violation or unfair or deceptive act or practice, and an opportunity for the facilitator to be heard. If, following the hearing, the Commissioner finds that an action of the facilitator is in violation of this Act or the rules or

¹⁸ See NCLC/CFA 2002 RAL Report at 12.

regulations promulgated thereunder or that the facilitator has engaged in an unfair or deceptive act or practice, the Commissioner shall order the facilitator to cease and desist from the action. The Commissioner may make investigations, subpoena witnesses, and require audits and reports, in preparation for such hearings, and shall make findings of fact and conclusions of law. All such hearings shall be open to the public.

If the facilitator continues to engage in an action in violation of the Commissioner's order to cease and desist from the action, the facilitator shall be subject to a penalty of one thousand dollars (\$1,000) for each action it takes in violation of the Commissioner's order.

(b) Revocation of Registration. After notice and hearing, and upon the finding that a registrant has (i) engaged in a course of conduct that is in violation of this Act or the rules or regulations promulgated thereunder or (ii) continued to engage in an action in violation of a cease and desist order of the Commissioner that has not been stayed upon application of the registrant, the Commissioner may revoke the registration of the registrant temporarily or permanently at the discretion of the Commissioner. No revocation, suspension, or surrender of any registration shall relieve the registrant from civil or criminal liability for acts committed prior thereto.

(c) Complaint Process. The Commissioner shall maintain a list of registrants which shall be available to interested persons and the public. The Commissioner shall create a toll-free telephone number whereby consumers may obtain information about registrants and complaint forms. The Commissioner shall establish a complaint process whereby an aggrieved consumer or any member of the public may file a complaint against a registrant or non-registrant who violates any provision of this Act. All complaints shall be considered public records pursuant to [cite for state public records law] with the exception of the complainant's name, address, or other personal identifying information. The Commissioner shall hold a hearing pursuant subsection (a) upon the request of a party to the complaint. The Commissioner may after such hearing issue cease and desist orders pursuant to subsection (a), or suspend or revoke a registration as provided in subsection (b).

Commentary

This section gives the Commissioner the power to impose penalties for violation of the Act. A single violation will result in a cease and desist order. Continuing violations will result in a civil penalty. This section also gives the Commissioner the power to revoke a facilitator's registration for continued violations of the Act. These provisions are similar to the administrative remedies in the North Carolina RAL statute, N.C. Gen. Stat. § 53-251.

This section requires the Commissioner to establish a complaint process for consumers. The complainant or the facilitator is entitled to seek a hearing on the complaint. This section gives the public the right of access to both the list of registrants and all complaints against registrants, except for the personal identifying information of complainants.

Section 10. **Private Right of Action**

(a) The remedies provided herein are cumulative and apply to registrants and to unregistered persons to whom this Act applies and who fail to register.

(b) Any violation by a facilitator of any state law prohibiting unfair or deceptive acts or practices constitutes a violation of this Act.

(c) Any violation of this Act constitutes a violation of any state law prohibiting unfair or deceptive acts or practices.

(d) Damages. A facilitator who fails to comply with any provision of this Act is liable to the consumer for: (i) actual and consequential damages; (ii) statutory damages of \$2,000 (to be increased annually based proportionally on changes in the Consumer Price Index, with fractional amounts rounded to the nearest dollar) or three times the amount of the refund anticipation loan fee or other unauthorized charge, whichever is greater; and (iii) reasonable attorney's fees and costs.

(e) Any person may sue for injunctive or other appropriate equitable relief to enforce this Act.

(f) Any consumer may bring a class action suit to enforce this Act. In any such class action, a facilitator who fails to comply with any provision of this Act is liable for: (i) actual and consequential damages for each class member; (ii) statutory damages as set forth in subsection (d)(ii) for each class member; and (iii) reasonable attorney's fees and costs.

(g) The remedies provided in this section are not intended to be the exclusive remedies available to a consumer nor must the consumer exhaust any administrative remedies provided under this Act or any other applicable law.

Commentary

The private right of action gives consumers the ability to enforce the provisions of the Act, allowing them to directly sue RAL and RAC facilitators, both registered and unregistered. A private right of action is essential to ensuring that the Act has a meaningful impact. Agency enforcement through the complaint process alone is sometimes inadequate, given the fact that many agencies do not have sufficient resources to investigate all violations and undertake enforcement actions. All of the current state RAL statutes have some form of private right of action. N.C. Gen. Stat. § 53-251(c); Minn. Stat. § 270.30(6); Ill. Comp. Stat. Ann. ch. 815, § 177/15; N.Y.C. Admin. Code § 20-743.1.

This section permits consumers to seek actual and consequential damages, including costs and attorney's fees. It also imposes a statutory penalty of \$2,000 per violation, or three times the RAL fee, whichever is greater. The statutory penalty is important because the actual damages in these cases may be small, and alone might not deter a business from violating this Act. The statutory penalty is indexed to the Consumer Price Index to prevent its deterrent effect from being eroded by inflation. Statutory penalties of this type are common in the federal consumer

protection acts. This section includes injunctive relief as another method of discouraging violations by businesses that may not be deterred by damage awards alone. For the same reason, and to assist groups of borrowers who have been injured by violation, this section includes a provision allowing for class actions.

Section 11. Rules

The Commission may adopt rules as necessary to effectuate the purpose of this Act, to provide for the protection of the borrowing public, and to assist facilitators in interpreting this Act. The Commission may modify the disclosures in subsections 5(c) and 6(d) to the extent that a revision of the 10 day estimate for receiving a refund from the Internal Revenue Service (with electronic filing and direct deposit) is appropriate.

Commentary

This Section gives the Commission the power to establish regulations to implement the Act. This Section also gives the Commission the power to modify the estimate of 10 days for an e-filed, direct deposit refund in the mandatory warnings at subsections 5(c) and 6(d). The IRS has stated that in a few years, it plans to reduce the amount of time for an e-filed, direct deposit refund to 3 or 4 days. If and when this reduction in time occurs, this section permits the Commission to modify the disclosures in subsection 5(c) and 6(d) to inform consumers of this improvement.

Section 12. Annual reports.

On or before July 1 of each year, beginning July ____, each facilitator shall file an annual report with the Commissioner pursuant to procedures that the Commissioner shall establish. An annual consolidated report shall be prepared by the Commissioner and made available to the public. These reports shall include the following information for the time period of April 15 of the prior year to April 15 of that year:

- (a) The total number and dollar amount of refund anticipation loans facilitated by the facilitator.
- (b) The total number and dollar amount of refund anticipation checks facilitated by the facilitator.
- (c) The average number of days for which refund anticipation loans facilitated by the facilitator were outstanding before being repaid.
- (d) The name and address of any creditor or person for whom the facilitator facilitates refund anticipation loans or refund anticipation checks.
- (e) Any other information required by the Commissioner.

Commentary

Facilitators must file an annual report in which they must list, among other things, the number of RALs and RACs, the volume of RALs and RACs in dollars, and the average loan period for the

RALs they facilitated. This information will be compiled by the Commissioner and made available to the public, the governor, and the legislature. This information is critical in gauging the status of the industry and in determining if the Act serves the purposes for which it is intended.

Section 13: Severability

If any portion of this Act is determined to be invalid for any reason by a final nonappealable order of any court of this state or of a federal court of competent jurisdiction, then it shall be severed from this Act. All other provisions of this Act shall remain in full force and effect.

Additional Provisions Regarding Advertising

The following is a model language for those interested in regulating RAL advertising:

For section 2 - "Definition"

"Market" or "advertise" shall mean to produce, distribute, broadcast, or otherwise display or have displayed written materials, oral statements, or visual materials describing the facilitator's products and services.

Section A. Advertising and Marketing

(a) No facilitator shall market or advertise a refund anticipation loan without including this language verbatim:

"[Name of product] is a loan. You can get your refund in about 10 days without a loan or extra fees if you use e-file and direct deposit."

For print advertisements, this information must be in type size one-half as large as the largest type size in the advertisement. For radio and television advertisements, this information must receive at least 7 seconds of airtime.

(b) No facilitator shall market or advertise a refund anticipation loan without including this language verbatim:

"The [name of product] costs [fee for RAC]. You can get your refund in about 10 days without this fee if you use e-file and direct deposit."

For print advertisements, this information must be in type size one-half as large as the largest type size in the advertisement. For radio and television advertisements, this information must receive at least 7 seconds of airtime.