



Children's Defense Fund

February 22, 2005

John Snow
Secretary of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

Eric Solomon
Assistant Secretary for Tax Policy(acting)
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

Mark W. Everson
Commissioner, Internal Revenue Service
Department of the Treasury
1111 Constitution Ave., NW
Washington, DC 20224

Dear Secretary Snow, Commissioner Everson and Assistant Secretary Solomon:

We write to you regarding the refund anticipation loan (RAL) study that Congress mandated in Section 221 of the Treasury Appropriations bill. We are requesting that advocates, such as the National Consumer Law Center, Consumer Federation of America, National Community Tax Coalition, and Children's Defense Fund, be given an opportunity to be part of the process in developing the study and issuing the report of its findings. In addition, the IRS should consult other experts on these topics, such as the Brookings Institution and Center on Budget and Policy Priorities.

Requests to Be Involved in Study Process

Collectively, the undersigned groups have spent years researching and working on the issue of RALs. Thus, it would be important, and we believe valuable, to have the input of our groups and the others mentioned above into the study design and drafting of the report. We understand that the IRS must conduct the study in consultation with the National Taxpayer Advocate, who represents the interests of taxpayers and has done an effective and aggressive job in so doing. Nevertheless, we believe we have a unique role and perspective, as well as valuable information, to offer those in the IRS working on the report.

As an initial matter, we would like to be consulted on the design, methodology, and techniques of the study. We also would like to meet with the staff conducting the study. When the study is completed, we request that we be given a copy of the draft report in time to make comments. Finally, we request that you automatically send us copies of any documents about the study that are being shared with commercial tax preparers and RAL lenders.

Suggestions for Information To Be Included in the Report

Section 221 of the Treasury Appropriations bill requires the IRS to issue a report on “the uses of the Debt Indicator tool, the debt collection offset practice, and recommendations that could reduce the amount of time required to deliver tax refunds. In addition, the report shall study whether the Debt Indicator facilitates the use of refund anticipation loan (RALs), evaluate alternatives to RALs, and examine the feasibility of debit cards being used to distribute refunds.”

Understandably, the language in Section 221 is fairly general in the topics required to be in the study. We believe there are important specific pieces of information that should be covered by the study in order for it to fulfill the purposes that Congress intended. These items of information with respect to the Debt Indicator program include:

- Has the use of the Debt Indicator actually lowered the cost of RALs over the years? This analysis should examine the actual fees charged for RALs since 1993 to the present, in comparison to inflation, real credit risk, and the transaction costs of making the loans.
- What is the monetary and non-monetary value to RAL lenders and commercial tax preparers of the Debt Indicator? How much does it reduce loan losses? What is the value to tax preparers and RAL lenders in terms of fewer phone calls, better customer satisfaction, and lower transaction costs?
- What does it cost the IRS to issue the Debt Indicator on a programmatic level and for each individual return? Is the IRS considering charging tax preparers for the Debt Indicator?
- Could the IRS send the Debt Indicator directly to individuals but not give it to third parties, such as RAL lenders or tax preparers? (In other words, could the taxpayer benefit from knowing there is a claim against his or her return without using this information as a credit reporting screen?)
- Do consumers know they have agreed to share this information with their tax preparer and with the RAL lender when they sign up for the loan? The IRS should conduct focus groups or polling of RAL users to determine this information.

With respect to RALs in general, we believe important topics that should be covered by the study include:

- An analysis of “pay stub loans,” *i.e.*, loans made to taxpayers prior to their receipt of their W-2 (pre-filing season). This analysis should include a breakdown of the prices that taxpayers pay for these loans, including whether the taxpayer takes out one or two loans. It should also explore whether those loans require the taxpayer to return to the same commercial preparer, and thus constitute “tying” arrangements.
- What is the profit for lenders on each RAL? (As part of this calculation, any cost estimates of delinquent RALs should include recoveries in successive years through cross lender debt collection.)
- Would federally established caps on RAL fees benefit RAL borrowers, especially EITC recipients?

With respect to cross-lender debt collection, the study should gather data and report on:

- How many delinquent RALs are collected through the cross collection method. How many RALs go into default in the year they are made but are collected in the next few years through cross collection?

- Do consumers understand that there is a risk of cross collection when they apply for a RAL? When they do find out about this risk, do consumers think cross collection is a fair tactic? Again, the IRS should conduct focus groups or polling of RAL users to determine this information.
- How many delinquent RALs are caused by the IRS freezing refunds? Does the IRS know and take into consideration that a frozen refund involves a RAL?

With respect to new refund delivery methods, the report should include information on:

- An evaluation of all stored value, debit and other cards that deliver the proceeds of the tax refunds or RALs.
- A comparison of trends in direct deposit of refunds over time.
- An examination of how to encourage partnerships between free tax preparation programs and credit unions/banks to make accounts available during tax season.
- An examination of the trends in unbanked status among EITC and child credit recipients.
- What factors or demographics influence whether taxpayers with bank accounts have refunds direct deposited? What kind of outreach and marketing can IRS do to urge people to get their money faster through direct deposit?

We also request that the IRS include certain information about its own activities in the report required by Section 221, including:

- What is the IRS doing to speed up delivery of refunds?
- What complaints have there been or investigations conducted on used car lots, check cashers, rent to own stores, and payday lenders who engaged in tax preparation and facilitate RALs? In particular, have there been any investigations to determine whether these non-traditional preparers have been following the IRS law on privacy of tax return information?
- If Congress authorized and funded such a program, how quickly could the IRS be ready to let taxpayers file their returns online directly with the IRS?

Conclusion

We urge the IRS to include advocates and others in the process and development of the RAL study required by Section 221 of the Treasury appropriation bill. We believe that our involvement will benefit taxpayers and the IRS. For example, representatives of some of our organizations have successfully worked with the IRS in the past in the development of VITA sites.

Thank you for your consideration of this matter. If you have any questions about this letter, please contact Chi Chi Wu at 617-542-8010.

Sincerely,

Chi Chi Wu
National Consumer Law Center
(on behalf of its low-income clients)

Jean Ann Fox
Consumer Federation of America

Gail Hillebrand
Consumers Union

Ed Mierzwinski
U.S. PIRG

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National Community Tax Coalition

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cc: Nina Olson, National Taxpayer Advocate
Alan Berube, Brookings Institution
John Wancheck, Center on Budget and Policy Priorities