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Consumers pay millions in fees for tax refund loans

When taking out a loan, most consumers will shop around at various financial institutions in order to find the best interest rate.

However, some taxpayers who are in a hurry to get their refund and take out tax refund loans pay an exorbitant amount of interest on these loans, said Sissy Osteen, Oklahoma State University Cooperative Extension Service resource management specialist.

“Also known as refund anticipation loans or instant refund loans, companies often target lower income tax payers by offering to get their tax refund within just a couple of days,” Osteen said. “However, the fees for an average refund of just under \$2,000 will equate to an annual percentage rate of 222.5 percent. Consumers with lower incomes often need their tax returns quickly, but this type of transaction is actually quite costly. Unfortunately, millions of taxpayers fall victim to these rip-offs. In fact, last year about 12 million taxpayers paid more than \$900 billion in fees just to get their refunds a little faster.”

Consumers need to know that there are no-cost or low-cost methods of getting quick tax returns. In 2002, the Internal Revenue Service instituted a new program that allows millions of Americans to have their tax return prepared and filed electronically at no cost. Seventeen companies provide these services through an alliance with the IRS. Eligibility does vary from one company to another but is based on factors such as age, adjusted gross income, and in some cases, state of residency. Consumers who qualify for Earned Income Tax Credit (EITC) make up only 15 percent of all taxpayers, but represented more than half of all refund anticipation loans in recent years.

“Most of these consumers didn’t even realize that they were actually taking out a loan,” Osteen said. “This lack of awareness, while costly, is extremely common. Anyone who files electronically can have their refund deposited directly into their bank accounts within about 10 days. Taxpayers who don’t have a bank account will have to wait a while longer to receive their check in the mail. Typically the earlier in the year you file, the sooner you get the refund.”

One way to put more money in each paycheck is to file a new W-4 form with an employer and claim more withholding allowances.

Consumers who find it difficult to hang on to money may want to consider changing their W-4 forms and having the money automatically deducted from the paycheck and directly deposited into a savings account.

“While it may be tempting to get a refund in about 48 hours, it’s not a good financial decision,” Osteen said. “Taxpayers who consider this option may need to sit down and reevaluate their financial situation in order to avoid falling prey to such high interest loans.”

Information prepared by Trisha Gedon, Communication Specialist OSU AG Communication Services.

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