

H&R Block's Refund Anticipation Loan: A Paradox of Profitability?

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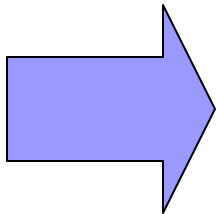
Profit – How much is too much?

Approaches


- Economic
- Philosophical
- Religious
- Political and governmental
- Consumer Advocates

Open Questions

- For what products?
- For what consumers?
- At what times?
- Under what circumstances?



Centuries Long Debate
Only thing for sure: Issues will be raised



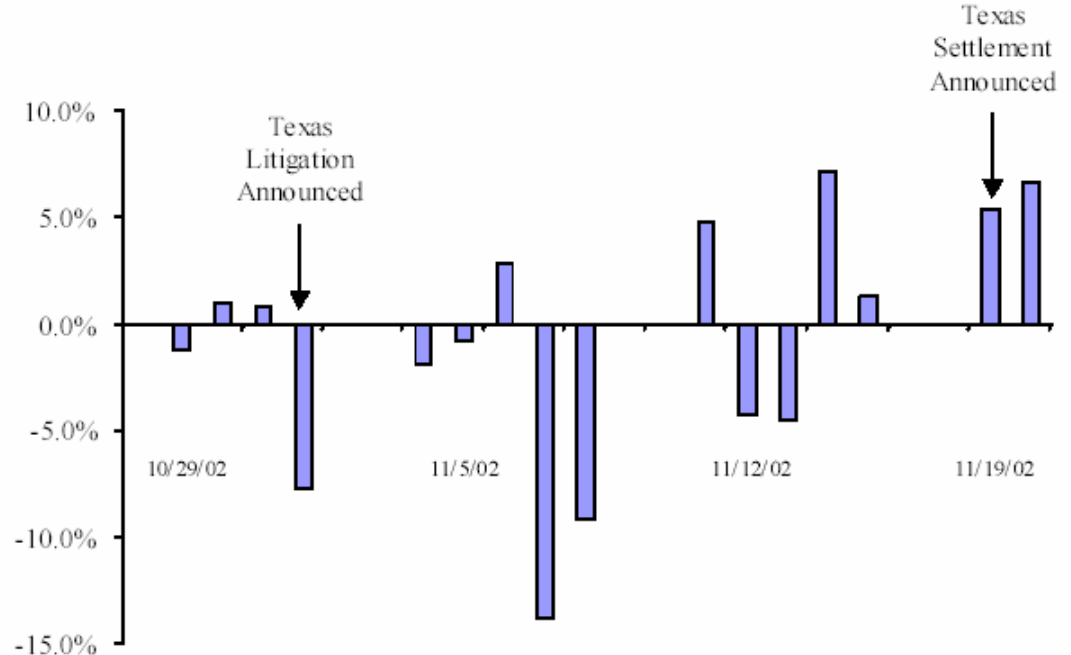
Block's experience with RALS; “a product that...consumers love...”

- Block is a \$4.2 billion financial services company
 - Main business is retail tax preparation; 57% of customers have household incomes below \$30,000
- Introduced the “Refund Anticipation Loan” (RAL) in 1986
 - Product allows customers to receive their federal refund in as little as 1-2 days versus several weeks
 - Annualized interest rates average over 90 percent
- RALs are highly demanded by customers and financially significant to Block
 - Block sells over four million RALs annually
 - Deliver over \$100 million in earnings annually (25 percent of total earnings)

...and “consumer groups hate”

- Over twelve (mostly class action) lawsuits with substantial payouts
- Uncertainty with respect to future earnings
- Strong criticism from advocacy groups
 - Contend that:
 - rates “too high”
 - Inadequate disclosure
 - ACORN
 - 2004 campaign against Block in 16 states
 - Generates significant negative publicity

H&R Block Stock Price, 10/29/02 – 11/19/02





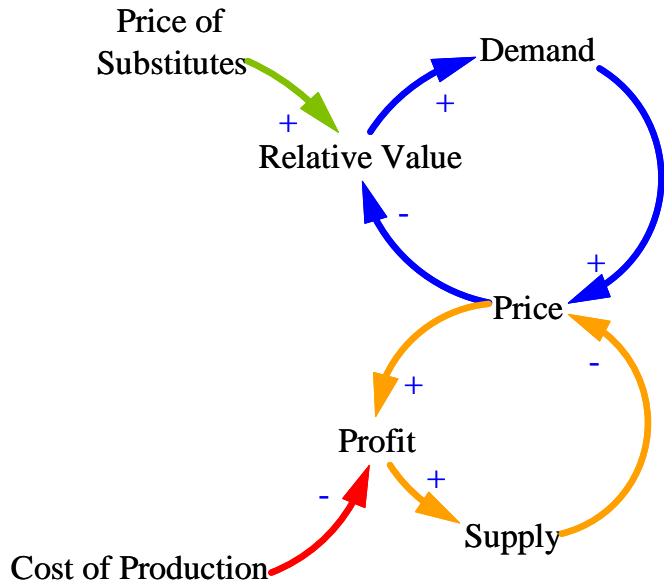
General proposition: Unintended consequences of “Voice”

- Albert Hirschman’s “Exit, Voice and Loyalty” (1970)
 - Consumers have the alternatives of “exit” and “voice”.
 - *Non-consumers* can only exercise “voice”
- These activities can affect both demand and supply
 - Demand: reduce interest by consumers
 - Supply: May increase supply (highlight BOP opportunities) or decrease supply (through direct increases in costs by firms.)

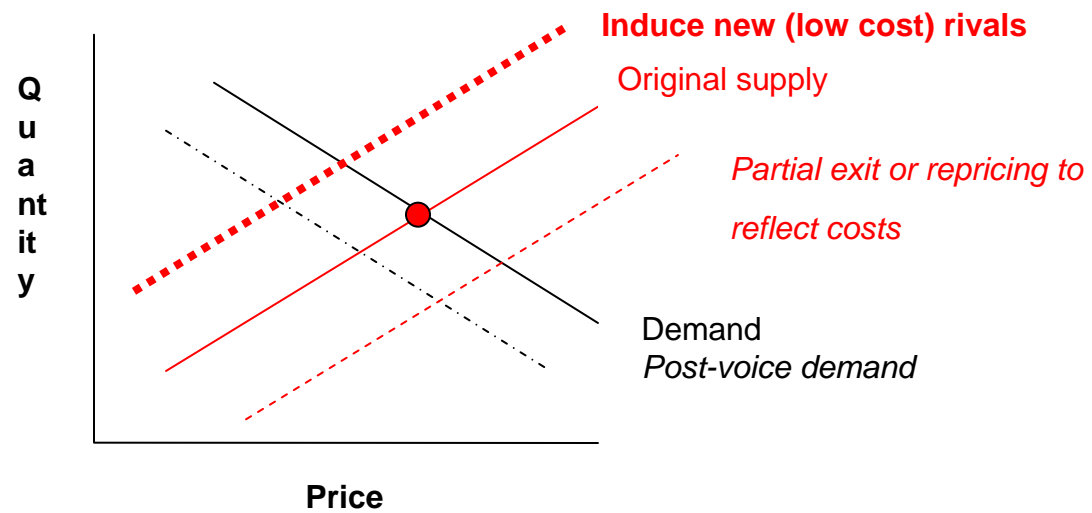
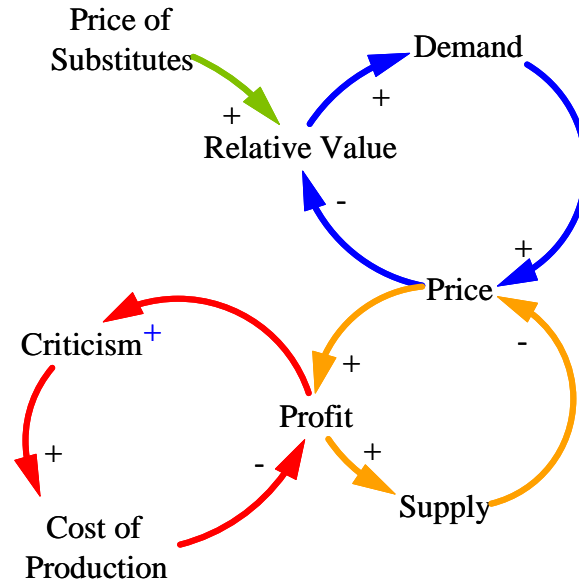
- May end up increasing prices for consumers
- If voice differentially targeted to large, profitable, highly visible firms, then comparative advantage given to small, less profitable, less visible firms.



Normal Feedback Structure of Markets



Feedback Structure With Added Scrutiny





Addressing the paradox

Leveraging the Debate

- Publicly identify BOP opportunities
- Positive voice for firms
- Confront the “profits debate” directly
- Use partnerships with non-profits
- Research the costs and benefits of voice activities

Block Examples

- Piloting new products and services. Openly discussing results
- Convening roundtables and discussions with consumer advocacy groups (CFA, ACORN)
- Partnering with highly visible and influential non-profits and policy-makers (Operation Hope, Cities of Miami and San Francisco)
- Sponsoring policy studies with Brookings, M.I.T., U.C. Berkeley and Harvard