

**H.R. 4181, THE DEBT PAY INCENTIVE ACT OF  
2000**

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**HEARING**  
BEFORE THE  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION, AND TECHNOLOGY  
OF THE  
COMMITTEE ON GOVERNMENT REFORM  
HOUSE OF REPRESENTATIVES  
ONE HUNDRED SIXTH CONGRESS

SECOND SESSION

ON

**H.R. 4181**

TO AMEND TITLE 31, UNITED STATES CODE, TO PROHIBIT DELINQUENT  
FEDERAL DEBTORS FROM BEING ELIGIBLE TO ENTER INTO FEDERAL  
CONTRACTS, AND FOR OTHER PURPOSES

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MAY 9, 2000  
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**H.R. 481, THE DEBT PAY INCENTIVE ACT OF  
2000**

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**TUESDAY, MAY 9, 2000**

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION, AND TECHNOLOGY,  
COMMITTEE ON GOVERNMENT REFORM,  
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10 a.m., in room 2154, Rayburn House Office Building, Hon. Stephen Horn (chairman of the subcommittee) presiding.

Present: Representatives Horn, Biggert, Davis, Ose, Turner, and Maloney.

Staff present: J. Russell George, staff director and chief counsel; Randy Kaplan, counsel; Bonnie Heald, director of communications; Bryan Sisk, clerk; Michael Soon and Elizabeth Seong, interns; Michelle Ash and Trey Henderson, minority counsels; and Jean Gosa, minority assistant clerk.

Mr. HORN. A quorum being present, the Subcommittee on Government Management, Information, and Technology will come to order.

Today we will examine a bill introduced by the ranking member of this subcommittee, Representative Jim Turner of Texas.

[The text of H.R. 4181 follows:]

106TH CONGRESS  
2D SESSION

# H. R. 4181

To amend title 31, United States Code, to prohibit delinquent Federal debtors from being eligible to enter into Federal contracts, and for other purposes.

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## IN THE HOUSE OF REPRESENTATIVES

APRIL 5, 2000

Mr. TURNER (for himself, Mr. HORN, Mr. BURTON of Indiana, Mr. WAXMAN, Mr. OWENS, Mrs. BIGGERT, Mrs. MALONEY of New York, Mr. WALDEN of Oregon, Mr. DAVIS of Virginia, Mr. OSE, Mr. TANNER, Mr. DOGGETT, Mr. MATSUI, Mr. SHAYS, Mr. MICA, Mr. STENHOLM, Mrs. MORELLA, Mr. THORNBERRY, Mr. GREEN of Texas, Mr. WAMP, Mr. BENTSEN, Mr. HUTCHINSON, Mr. LAMPSON, Mr. BACHUS, Mr. TIERNEY, Mr. PITTS, Mr. HALL OF TEXAS, and Mr. GILMAN) introduced the following bill; which was referred to the Committee on Government Reform, and in addition to the Committee on Ways and Means, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned

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## A BILL

To amend title 31, United States Code, to prohibit delinquent Federal debtors from being eligible to enter into Federal contracts, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*  
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the "Debt Payment Incen-  
5 tive Act of 2000".

1 **SEC. 2. AMENDMENTS TO PROVISION REGARDING DELIN-**  
2 **QUENT FEDERAL DEBTORS.**

3 Section 3720B of title 31, United States Code, is  
4 amended:

5 (1) in the section heading, by adding at the end  
6 **“or contracts”**;

7 (2) in subsection (a):

8 (A) by inserting “or be eligible to enter  
9 into a Federal contract with the agency” after  
10 “administered by the agency”;

11 (B) by inserting “, including” after “debt”  
12 the first place such term appears;

13 (C) by striking “(other than” the second  
14 place such words appear;

15 (D) by striking the closing parenthesis  
16 after “1986”; and

17 (E) by inserting “and be eligible to enter  
18 into Federal contracts” after “loan guaran-  
19 tees”; and

20 (3) by adding at the end the following:

21 “(c)(1) The head of any Federal agency that admin-  
22 isters a Federal loan or loan guarantee program or that  
23 issues a request for proposals for a Federal contract shall  
24 require each applicant for a Federal loan or loan guar-  
25 antee and each entity that submits a proposal to enter  
26 into a contract with the agency to submit with the loan

1 or loan guarantee application or the contract proposal a  
2 form authorizing the Secretary of the Treasury to disclose  
3 to the head of the agency information describing whether  
4 the applicant or prospective contractor has an outstanding  
5 debt under the Internal Revenue Code of 1986 in delin-  
6 quent status.

7       “(2) Not later than 30 days after the date of the en-  
8 actment of this subsection, the Secretary shall develop and  
9 make available to all Federal agencies a standard form,  
10 the purpose which shall be to authorize the disclosure de-  
11 scribed in paragraph (1).

12       “(d) For purposes of this section:

13           “(1) The term ‘contract’ means a binding  
14 agreement entered into by a Federal agency for the  
15 purpose of obtaining supplies, materials, equipment,  
16 or services, but does not include

17           “(A) a contract to assist the agency in the  
18 performance of disaster relief authorities, as  
19 designated in standards prescribed by the Sec-  
20 retary of the Treasury; or

21           “(B) a contract designated by the Presi-  
22 dent as necessary to the national security of the  
23 United States.

24       “(2) The term ‘person’ includes

1           “(A) any partnership with a partner who  
2           has been assessed a penalty under section 6672  
3           of the Internal Revenue Code of 1986 with re-  
4           spect to a debt which is in delinquent status as  
5           described in paragraph (3); and

6           “(B) any corporation with an officer or a  
7           shareholder who holds 25 percent or more of  
8           the outstanding shares of corporate stock in  
9           that corporation who has been assessed a pen-  
10          alty under section 6672 of the Internal Revenue  
11          Code of 1986 with respect to a debt that is in  
12          delinquent status as described in paragraph (3).

13          “(3) A debt under the Internal Revenue Code  
14          of 1986 shall be considered to be in delinquent sta-  
15          tus if it has not been paid within 90 days of an as-  
16          sessment of a tax, penalty, or interest under the In-  
17          ternal Revenue Code of 1986. Such a debt does not  
18          include a debt that is being paid in a timely manner  
19          pursuant to an agreement under section 6159 or  
20          section 7122 of the Internal Revenue Code of  
21          1986.”.

Mr. HORN. Mr. Turner's bill is a superb one as far as I am concerned, and I am glad to be a cosponsor of it. H.R. 4181, the Debt Payment Incentive Act of 2000 would prohibit delinquent tax debtors from receiving Federal loans or contracts until their delinquencies are resolved.

The bill expands the Debt Collection Improvement Act of 1996, which bars delinquent nontax debtors from receiving Federal loans or loan guarantees. That law only applied to non-tax related delinquent debts. Frankly, the reason it applied only to that is that if we wanted the bill to get through in 1996 we had to ride the train leaving the station, and that meant don't get bogged down in the Committee on Ways and Means.

These overdue debtors that are referred to in the nontax-related delinquent debts, who are overdue in paying off their student loans and home mortgages, farm or business loans, currently owe the Federal Government a total of \$46 billion. However, the 1996 law does not apply to the tax-related debt, as we noted, which is estimated to be \$231 billion in overdue taxes, penalties, and interest.

At a hearing last summer, the General Accounting Office testified that unpaid payroll taxes is one of the largest categories of that outstanding tax debt. GAO investigators found that nearly 2 million business owners owed the Federal Government nearly \$50 billion in unpaid payroll taxes, taxes these employers had collected from their workers but failed to forward to the U.S. Treasury.

Despite those debts, however, a significant number of the same business owners and other individuals with delinquent tax debts are receiving millions of dollars in Federal benefits and new loans. H.R. 4181 would prohibit that outrageous practice from continuing. The bill would require the Internal Revenue Service to report the tax status of all applicants for Federal loans, loan guarantees, and Federal contracts to the agency granting the loan or issuing the contract.

Admittedly, this places an additional administrative responsibility on an agency, the Internal Revenue Service, and that agency, as we know, is already beleaguered by serious financial and operational challenges, but that cannot be any excuse for picking up the nontax debt and the tax debt.

Today we will examine whether the Internal Revenue Service can meet this responsibility.

We will also hear from representatives of other Federal agencies who will discuss their views on the legislation. I commend Mr. Turner for seeking to remedy this appalling abuse of taxpayers' money and yield to him to discuss his bill.

[The prepared statement of Hon. Stephen Horn follows:]

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**Hearing on H.R. 4181, the "Debt Pay Incentive Act of 2000"**  
**CHAIRMAN STEPHEN HORN (R-CA)**  
**OPENING STATEMENT**  
**Tuesday, May 9, 2000**

A quorum being present, the Subcommittee on Government Management, Information, and Technology will come to order.

Today, we will examine a bill introduced by the ranking member of this subcommittee Representative Jim Turner from Texas. Mr. Turner's bill, H.R. 4181, the "Debt Pay Incentive Act" would prohibit delinquent tax debtors from receiving federal loans or contracts until their delinquencies are resolved.

The bill expands the Debt Collection Improvement Act of 1996, which bars delinquent non-tax debtors from receiving federal loans or loan guarantees. That law applies only to non-tax related delinquent debts. These debtors, who have failed to repay their student loans, home mortgages, or farm or business loans, currently owe the government \$46 billion.

The 1996 law does not apply to those who fail to pay their tax-related debts, which is estimated to be about \$231 billion in taxes, penalties and interest.

At a hearing last summer, the General Accounting Office testified that unpaid payroll taxes is one of the largest categories of that outstanding tax debt. GAO investigators found that nearly 2 million business owners owed the federal government nearly \$50 billion in unpaid payroll taxes -- taxes these employers had collected from their workers but failed to forward to the U.S. Treasury. Despite those debts, a significant number of the same business owners -- and other individuals with delinquent tax debts -- are receiving billions of dollars in federal benefits and new loans.

H.R. 4181 would prohibit that egregious practice from continuing. The bill would require the Internal Revenue Service to report the tax status of all applicants for federal loans, loan guarantees and federal contracts to the agency granting the loan or issuing the contract. Admittedly, this places an additional administrative responsibility on an agency that is already beleaguered by serious financial and operational challenges. Today, we will examine whether the IRS can meet this responsibility. We will also hear from representatives of other federal agencies who will discuss their views on the legislation.

I commend Mr. Turner for seeking to remedy this appalling abuse of taxpayers' money, and yield to him to discuss his bill.

Mr. HORN. Mr. Turner.

Mr. TURNER. Thank you, Mr. Chairman.

First of all, I want to thank you for granting a hearing to this bill; and I thank you for your cosponsorship of the legislation. I also want to thank Mr. Davis and Mr. Ose who have joined with us, along with Mr. Burton, Mr. Waxman, Mr. Owens, Mrs. Biggert, Mrs. Maloney, Mr. Walden of our committee; also, I thank Mr. Shays and Mr. Mica, Mr. Tierney, Mr. Gilman, on our full committee, have joined with us in this effort.

It is no secret that taxpayers owe the Federal Government billions of dollars in delinquent taxes, and to figure out how to collect that is one of the tasks that this committee under Chairman Horn's leadership has struggled with on many fronts.

According to the IRS records, the Federal Government was owed \$231 billion in unpaid taxes, penalties, and interest. In a hearing before this subcommittee in August of last year, the General Accounting Office revealed that nearly 2 million businesses owed \$49 billion in cumulative unpaid payroll taxes. An additional \$15 billion in penalties had been assessed against the 185,000 individuals responsible for the nonpayment of these payroll taxes.

The GAO also reported that a significant number of businesses with unpaid payroll taxes and individuals with outstanding penalties are also receiving billions of dollars in Federal benefits. One alarming example was of a freight handler company which owed an estimated \$2 million in unpaid payroll taxes. They routinely funneled corporate funds to an affiliated company, one owned by one of the corporate officers, to acquire trucks and other equipment for the affiliated company's expansion. Eventually it turned out the IRS discovered that funds for the unpaid payroll taxes were also being used for corporate officers' personal expenses, including the installation of a private swimming pool and maintenance of at least eight antique cars owned by one of the corporate officers. The most disturbing aspect of this story is the fact that during this time Federal contracts accounted for 85 percent of this particular company's revenues.

Additionally, we learned that about 12,500 taxpayers, both businesses and individuals with outstanding payroll liabilities totaling about \$280 million, had received SBA loan disbursements totaling about \$2.4 billion.

In a 1992 GAO report that studied 26,000 businesses that had Federal contracts valued at over \$25,000, the GAO discovered that 21 percent or more than 5,700 of these Federal contractors owed \$773 million in delinquent taxes, interest, and penalties, and another 4 percent of them, almost 1,100 of these Federal contractors, were under investigation for not filing Federal tax returns.

Can you believe that tax debtors enjoy Federal contracts and Federal loan assistance? They can under current law, and this legislation intends to change it.

We introduced this bill, H.R. 4181, the Debt Payment Incentive Act of 2000, to remedy this problem. This bipartisan legislation builds upon the success of the Debt Collection Improvement Act of 1996 which banned Federal loans and loan guarantees to delinquent nontax debtors.

H.R. 4181 amends the Debt Collection Improvement Act to bar delinquent Federal debtors from obtaining Federal contracts, as well as Federal loan assistance already covered under existing law. The bill expands the Debt Collection Improvement Act to include tax debt in generally the same manner that nontax debt is already included under the provisions of the Debt Collection Act. This is the first time tax debt has been brought under Federal law.

Strong precedent already exists for this legislation. OMB Circular A-129 already requires that Federal agencies determine whether applicants for Federal loan assistance are delinquent on any Federal debt, including tax debt.

Under this circular, agencies must include a question on loan application forms asking applicants if they have such delinquencies. Processing of applications should be suspended until the debtor satisfactorily resolves the debt. However, implementation of Circular A-129 has been uneven and the GAO reported that many agencies are not even following the requirements.

While I think we can all agree that those who fail to pay their taxes should not receive these Federal benefits, loans, and Federal contracts, I realize that there are a number of implementation issues surrounding the legislation.

I want to thank the numerous individuals and organizations who have submitted testimony and suggestions on our legislation: The U.S. Chamber of Commerce, the National Farmers Union, the Aerospace Industries Association, the National Defense Industry Association, National Federation of Independent Businesses, the National Taxpayers Union, the Small Business Administration, the Department of the Treasury, the IRS, the USDA, the GSA, of course the GAO, OMB, the Financial Management Services, the Department of Defense, and the Family Farm Coalition all commented or are prepared to testify regarding this legislation.

In an effort to find a workable solution to the problem that we have discussed, each of these people have been very open, each of these groups, in trying to offer their best assistance to achieve the goal that we all agree upon.

First, I recognize that the IRS is currently modernizing its computer systems; and a few weeks ago at our hearing, I asked Commissioner Rossotti to comment on this bill. He concluded that the IRS could handle the requirements of this new legislation if they were given time to implement the system to make it workable.

Therefore, it seems to me that the effective date of this legislation should take into account that there should be some lag time to be sure the IRS can handle this responsibility.

It is not the intent of this bill to delay the process by which the Federal Government awards contracts or loans, and it has also been suggested that perhaps during this interim period before the legislation becomes fully effective that a pilot project should be initiated, to be sure that it is workable and that the IRS can handle the task.

Second, with regards to procurement I still believe that making tax compliance is a prerequisite to awarding Federal contracts and that it is a legitimate screening tool. Currently, Federal agencies can consider tax delinquency in making their contract awards. Under this legislation, the agency head and the Treasury can waive

the bar to contracts. It is worthy of consideration that perhaps our legislation should delegate this responsibility to the chief procurement officer rather than solely being an authority granted to the agency head.

Third, I think it is important for us to be sure that our definition of delinquency will cover those who are still involved in legitimate disputes with the IRS. It has been suggested that perhaps our definition should have some refinement, and I am certainly open to the suggestions that will be made today to accomplish that.

We do not want to take any right of appeal away from any taxpayer by this legislation. We simply want to be sure that after all appeals and remedies are exercised by the taxpayer that if they still owe the Federal Government taxes, then they are barred from Federal contracts or loans.

Fourth, in order to clear up any confusion about what type of acquisitions are covered under this legislation, I would suggest, and it has been suggested, that we exempt small purchases under \$2,500 which under current law do not require a formal contract.

Fifth, with regard to the provisions relating to the penalties for trust fund taxes, it has been suggested that perhaps we should limit coverage of this bill to only partners with 25 percent ownership or more. I had originally suggested perhaps 10 percent. I am certainly open on that point as well.

In closing, let me make one final point. There are usually multiple policy goals involved when the Federal Government makes a loan or contract for services. One goal, it seems to me, should be to ensure that applicants applying for loans and businesses contracting with the government are not delinquent in their taxes. Exactly how we achieve that goal is the subject of this hearing today, and I welcome the testimony from each of our witnesses and again I thank the Chairman and the members of this committee who have joined in cosponsoring this bill. Thank you, Mr. Chairman.

[The prepared statement of Hon. Jim Turner follows:]

Statement of the Honorable Jim Turner  
GMIT Legislative Hearing: "H.R. 4181, The Debt Payment Incentive  
Act of 2000"  
5/9/00

Thank you, Mr. Chairman. It is no secret that taxpayers owe the federal government billions of dollars in delinquent taxes. According to recent IRS records, the federal government was owed \$231 billion in unpaid taxes, penalties, and interests. In an August 1999 hearing before this Subcommittee, the GAO revealed that nearly 2 million businesses owed \$49 billion in cumulative unpaid payroll taxes. An additional \$15 billion in penalties had been assessed against the 185,00 individuals responsible for the nonpayment of payroll taxes are still owed.

GAO also reported that a significant number of businesses with unpaid payroll taxes and individuals with outstanding penalties are also receiving billions of dollars in federal benefits. In one alarming example, a freight handler company, which owed an estimated \$2 million in unpaid payroll taxes, routinely funneled corporate funds to an affiliated company -- owned by one of the corporate officers -- to acquire trucks and other equipment for the affiliated company's expansion. Eventually, the IRS determined that funds for the unpaid payroll taxes were also being used for corporate officers' personal expenses, including the installation of a private swimming pool and

maintenance of at least eight antique cars owned by a corporate officer. The most disturbing aspect of this story is the fact that during this time federal contracts accounted for up to 85% of that company's revenue.

Additionally, we learned about 12,500 taxpayers (both businesses and individuals), with outstanding payroll tax liabilities totaling about \$280 million, had received SBA loan disbursements totaling about \$2.4 billion. A 1992 GAO report also found that 26,000 businesses had federal contract actions over \$25,000. According to IRS' records, twenty-two percent, or more than 5,700, of these federal contractors owed \$773 million in delinquent taxes, interest, and penalties, and another four percent, or almost 1,100, were under investigation for not filing tax returns.

Can you believe that tax debtors can enjoy federal contracts and loan assistance? They can under current law and we need to change it.

Therefore, I introduced, along with my colleague Chairman Horn and other members of this Committee, H.R. 4181, The Debt Payment Incentive Act of 2000. This bipartisan legislation builds upon the success of the Debt Collection Improvement Act of 1996, which banned federal loans and loan guarantees to delinquent non-tax debtors. H.R. 4181 amends the DCIA to bar delinquent federal debtors from obtaining

federal contracts as well as federal loan assistance which is already covered under the law. The bill expands the DCIA to include tax debt in generally the same manner that non-tax debt is already included under the barring provision of the DCIA. This is the first time tax debt has been brought under the DCIA.

Strong precedent already exists for this legislation. OMB Circular A-129 already requires that federal agencies determine whether applicants for federal loan assistance are delinquent on any federal debt, including tax debt. Under this circular, agencies must include a question on loan application forms asking applicants if they have such delinquencies. Processing of applications should be suspended until the debtor satisfactorily resolves the debt. However, implementation of Circular A-129 has been uneven, and the GAO reported that many agencies are not following its requirements.

While I think we can all agree that those who fail to pay their taxes should not receive these type of federal benefits, I realize that there are a number of implementation issues surrounding this bill. In an effort to find a workable solution, before we start this hearing, I wanted to enumerate the changes I would make to address some of the implementation concerns:

First, I recognize that the IRS is currently modernizing its computer systems. However, Commissioner Rossotti stated before this Subcommittee that the IRS could handle this bill in the long term if they were given time to get their system together. Therefore, I am willing to delay implementation of this bill until the IRS has had adequate time to ensure that its data base can be assembled so that it can administer this program in a timely and efficient manner. It is not the intent of this bill to delay the process by which the federal government awards contracts or loans. I would also consider a pilot in the interim.

Second, with regards to procurement, I still believe that making tax compliance a prerequisite for awarding federal contracts is a legitimate screening tool. Currently, federal agencies can consider tax delinquencies in making their contract award decisions. While I am not willing to remove the H.R. 418's bar against a delinquent contractor, I am willing to consider allowing the procurement officer the discretion to waive the bar.

Third, I want to know if our definition of delinquency will cover those who are still involved in a legitimate dispute with the IRS, and if so, I want to know what the right definition should be. I believe that 90 days is adequate time for the delinquent taxpayer to resolve his or her

liability after they have received a timely notice of their assessment. I am not very sympathetic to the taxpayer who has received adequate notice, yet has either negligently or intentionally failed to take steps to resolve his or her debt. I do not think that is the type of profile which we would want our applicants for federal loans or contracts to have. However, I would be willing to consider writing into the bill a provision which would allow the Treasury some flexibility to promulgate regulations to clarify this issue.

Fourth, in order to clear up any confusion about what type of acquisitions are covered under H.R. 4181, I am willing to exempt micro-purchases of under \$2500 which do not require a contractual vehicle.

Fifth, with regard to the provisions relating to the responsible person penalties for Trust Fund Taxes, I willing to possibly limit coverage of this bill to only partners with 10% ownership or more. By limiting the scope of this provision to partners with 10% or more, we will avoid the administrative burden of having to survey a large partnership.

In closing, I would like to make one final point. There are usually multiple public policy goals involved when the federal government makes a loan or contracts for goods and services. One goal, from my

perspective, should be to better ensure that the applicants applying for loans and the businesses contracting with the government are not delinquent in their taxes. Exactly how this goal should be balanced against others is a matter that needs to be worked out, but to ignore it would be a mistake.

Mr. HORN. Thank you very much for that summary of your legislation. The further opening statements will be limited to 5 minutes. We give the author more leeway. And I am delighted now to call on the Representative from Northern Virginia, Mr. Davis.

Mr. DAVIS. I have no comments.

Mr. HORN. I now call on Mrs. Maloney, Representative from New York, if she has any opening comments for 5 minutes.

Mrs. MALONEY. I support this legislation, and it is part of the continuum work that you and I have done together on working together to make government be more responsible and effective for the taxpayer and the citizens. I am glad to be here in support of this legislation. Thank you. I yield back my time.

Mr. HORN. We thank you. The gentleman from California, Mr. Ose.

Mr. OSE. No, sir.

Mr. HORN. OK. We will then start with the first panel. Let me just note for some of you that might not have been here before, we will ask you all and any of your assistants that are there that might whisper in your ear to take the oath when I have you stand on that. Then those that have written records, they will go in the hearing record at the point in which you are introduced on the panel. They will automatically be in there. I don't have to go through this mumbo-jumbo with every witness.

Then we would like you to keep your oral testimony to, let's say, 7 minutes or so, and we might give a little more leeway to the General Accounting Office because of the study here, but it is important that we get out the summary of your testimony on behalf of either the administration, the agencies, the GAO, so that we can have a dialog and then we will try to get everybody involved. So let us stand and raise your right hands and swear you in and your assistants. The clerk will count the people in the back row which are one, two, three, four, five backing up and then six witnesses.

[Witnesses sworn.]

Mr. HORN. The clerk will note that the six witnesses have affirmed and so have the assistants.

So we will start down the line in the order in which individuals are put on here, and that is with Cornelia M. Ashby, the Associate Director, Tax Policy and Administration Issues for the General Accounting Office.

Ms. Ashby is accompanied with Gregory D. Kutz, the Associate Director, Governmentwide Accounting and Financial Management Issues, and Tom Armstrong, the assistant general counsel. So Ms. Ashby.

**STATEMENTS OF CORNELIA M. ASHBY, ASSOCIATE DIRECTOR, TAX POLICY AND ADMINISTRATION ISSUES, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY GREGORY D. KUTZ, ASSOCIATE DIRECTOR, GOVERNMENTWIDE ACCOUNTING AND FINANCIAL MANAGEMENT ISSUES, AND TOM ARMSTRONG, ASSISTANT GENERAL COUNSEL; DEIDRE LEE, ACTING DEPUTY DIRECTOR FOR MANAGEMENT, OFFICE OF MANAGEMENT AND BUDGET; JOE MIKRUT, TAX LEGISLATIVE COUNCIL, DEPARTMENT OF THE TREASURY; CAROL COVEY, DEPUTY DIRECTOR OF DEFENSE PROCUREMENT, DEPARTMENT OF DEFENSE; AND SALLY THOMPSON, CHIEF FINANCIAL OFFICER, DEPARTMENT OF AGRICULTURE**

Ms. ASHBY. Mr. Chairman and members of the subcommittee, we are pleased to be here today to assist the subcommittee in its consideration of H.R. 4181. Our remarks are based on work we did for the subcommittee on unpaid payroll taxes and associated tax penalties and our audits of IRS.

We support the concept of barring delinquent taxpayers from receiving Federal contracts and loan assistance. However, with respect to H.R. 4181, we believe there are significant implementation issues involving the capability of IRS' current information systems, additional burden on the Federal acquisition process and using 90 days after assessment as the only determinant of delinquent status.

First, let me describe the current situation. As we reported to this subcommittee last August and as you mentioned earlier, Mr. Chairman, nearly 2 million businesses owed \$49 billion in delinquent unpaid payroll taxes as of September 30, 1998; and 185,000 individuals responsible for the nonpayment of delinquent payroll taxes owed \$15 billion in tax fund recovery penalties. Nearly 50 percent of the businesses were delinquent for more than one tax period, and nearly 25,000 individuals with trust fund recovery penalties had been assessed such penalties for more than one business.

Further, the majority of the unpaid payroll taxes and the associated trust fund recovery penalties are not likely to be collected. A significant number of businesses with delinquent unpaid payroll taxes and individuals with outstanding trust fund recovery penalties also receive substantial payments from the Federal Government. For example, our analysis indicated that as of September 30, 1998, over 1,700 businesses and individual taxpayers had received SBA loans estimated at nearly \$449 million after accumulating unpaid payroll tax delinquencies of almost \$32 million.

Against this backdrop, H.R. 4181 may provide several benefits. The general barring provisions of the bill would prevent delinquent taxpayers from benefiting from Federal loan assistance or contracts. Other provisions of the bill would end the practice by some multiple tax offenders of using Federal loans and contracts to start new businesses while the payroll taxes of other businesses they were or are associated with remain unpaid because of some willful action on their part.

In addition, the provisions of the bill could serve as an incentive for individuals and businesses to comply with their tax obligations. Also, the bill would provide fairness to compliant taxpayers who consistently fulfill their tax obligations while a portion of their tax

payments are used to finance Federal loans and contracts for those who do not pay their fair share.

However, accompanying these potential benefits are three implementation issues. First, IRS currently does not have the systems that would enable it to consistently provide Federal agencies with timely and accurate information on a taxpayer's delinquency status. IRS is undergoing a major systems modernization program which will likely take several more years to complete. If modernization efforts are successful, IRS may be able to provide accurate, real time delinquency status information.

OMB currently directs administrators of Federal loan assistance programs to determine whether an applicant has delinquent Federal debt, including tax debt, to assess creditworthiness. Because of this directive, agencies should have time built into their application processes to determine whether a loan applicant has Federal tax debt. Even so, because of IRS's limitations, we recommend that Congress provide that H.R. 4181 requirements be implemented on a pilot basis for one or more loan assistance programs to determine whether IRS' current systems could effectively and efficiently handle the expected volume of delinquency status requests.

The second implementation issue involves the Federal acquisition process. In recent years, both Congress and the administration have attempted to streamline the government procurement system in an effort to reduce costs. Because Federal agencies do not currently have to check a prospective contractor's tax delinquency status, H.R. 4181 could add considerable burden to the acquisition process. However, this burden could decrease if IRS' modernization efforts allow a real time tax delinquency check system. To help reduce the burden on the acquisition process, we recommend that Congress defer the application of the barring provisions of H.R. 4181 for Federal contracts until the results of the pilot program for loan assistance and IRS' systems modernization efforts are known.

The third implementation issue is a definitional one. Generally, with the exception of taxpayers that have made arrangements with IRS to make payments on their debts, H.R. 4181 would deny loan assistance or contracts to all taxpayers with tax debts that have been outstanding for more than 90 days after the date of assessment. As a starting point, the 90 days after assessment standard is not unreasonable. However, this provision may be too restrictive because it may not allow enough time for taxpayers to fully exercise their due process rights for collection actions or to negotiate payment agreements.

To help ensure that taxpayers are not barred from receiving Federal contracts or loan assistance prematurely, we recommend that the Congress require the Secretary of the Treasury to prescribe additional standards for IRS to use in determining when a taxpayer has a tax debt in delinquent status for purposes of barring under H.R. 4181.

Mr. Chairman, this concludes our statement. We would be pleased to answer any questions you or members of the subcommittee may have.

Mr. HORN. Thank you very much. We appreciate that very thorough statement.

[The prepared statement of Ms. Ashby follows:]

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to assist the Subcommittee in its consideration of H.R. 4181. My remarks are based on work we did for the Subcommittee on unpaid payroll taxes and associated tax penalties and our audits of IRS.

We support the concept of barring delinquent taxpayers from receiving federal contracts and loan assistance. However, with respect to H.R. 4181, we believe there are significant implementation issues involving the capability of IRS' current information systems, additional burden on the federal acquisition process, and using 90-days-after-assessment as the only determinant of delinquent status.

Potential Benefits of H.R. 4181

First, let me describe the current situation. As we reported to this Subcommittee last August, nearly 2 million businesses owed \$49 billion in delinquent unpaid payroll taxes as of September 30, 1998, and 185,000 individuals responsible for the nonpayment of delinquent payroll taxes owed \$15 billion in trust fund recovery penalties. Nearly 50 percent of the businesses were delinquent for more than one tax period, and nearly 25,000 individuals with trust fund recovery penalties had been assessed such penalties for more than one business. Further, the majority of the unpaid payroll taxes and the associated trust fund recovery penalties are not likely to be collected. A significant number of businesses with delinquent unpaid payroll taxes and individuals with outstanding trust fund recovery penalties also receive substantial payments from the

federal government. For example, our analysis indicated that, as of September 30, 1998, over 1700 business and individual taxpayers had received SBA loans estimated at nearly \$449 million after accumulating unpaid payroll tax delinquencies of almost \$32 million.

Against this backdrop, H.R. 4181 may provide several benefits. The general barring provisions of the bill would prevent delinquent taxpayers from benefiting from federal loan assistance or contracts. Other provisions of the bill would end the practice by some multiple tax offenders of using federal loans and contracts to start new businesses while the payroll taxes of other businesses they were or are associated with remain unpaid because of some willful action on their part. In addition, the provisions of the bill could serve as an incentive for individuals and businesses to comply with their tax obligations. Also, the bill would provide fairness to compliant taxpayers who consistently fulfill their tax obligations, while a portion of their tax payments are being used to finance federal loans and contracts for those who do not pay their fair share.

#### Implementation Issues

However, accompanying these potential benefits are 3 key implementation issues. First, IRS currently does not have the systems that would enable it to consistently provide federal agencies with timely and accurate information on a taxpayer's delinquency status. IRS is undergoing a major systems modernization program, which will likely take several more years to complete. If modernization efforts are successful, IRS may be able to provide accurate, real-time delinquency status information.

OMB currently directs administrators of federal loan assistance programs to determine whether an applicant has delinquent federal debt, including tax debt, to assess creditworthiness. Because of this directive, agencies should have time built into their application processes to determine whether a loan applicant has federal tax debt. Even so, because of IRS' systems limitations, we recommend that the Congress provide that H.R. 4181 requirements be implemented on a pilot basis for one or more loan assistance programs to determine whether IRS' current systems could effectively and efficiently handle the expected volume of delinquency status requests.

The second implementation issue involves the federal acquisition process. In recent years, both Congress and the administration have attempted to streamline the government procurement system in an effort to reduce its cost. Because federal agencies do not currently have to check a prospective contractor's tax delinquency status, H.R. 4181 could add considerable burden to the acquisition process. However, this burden could decrease if IRS' modernization efforts allow a real-time tax delinquency check system. To help reduce the burden on the acquisition process, we recommend that the Congress defer the application of the barring provisions of H.R. 4181 for federal contracts until the results of the pilot program for loan assistance and IRS' systems modernization efforts are known.

The third implementation issue is a definitional one. Generally, with the exception of taxpayers that have made arrangements with IRS to make payments on their debts, H.R. 4181 would deny loan assistance or contracts to all taxpayers with tax debts that have been outstanding for more than 90 days after the date of assessment. As a starting point,

the 90 days after assessment standard is not unreasonable. However, this provision may be too restrictive because it may not allow enough time for taxpayers to fully exercise their due process rights for collection actions or to negotiate payment agreements. To help ensure that taxpayers are not barred from receiving federal contracts or loan assistance prematurely, we recommend that the Congress require the Secretary of the Treasury to prescribe additional standards for IRS to use in determining when a taxpayer has a tax debt in delinquent status for purposes of barring under H.R. 4181.

Mr. Chairman, this concludes my statement. I would be pleased to answer any questions you or members of the Subcommittee may have.

United States General Accounting Office

**GAO**

**Testimony**

Before the Subcommittee on Government Management,  
Information, and Technology  
Committee on Government Reform  
House of Representatives

For Release on Delivery  
Expected at  
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**DEBT COLLECTION**

**Barring Delinquent  
Taxpayers From Receiving  
Federal Contracts and  
Loan Assistance**

Statement of Cornelia M. Ashby  
Associate Director, Tax Policy and Administration Issues  
General Government Division  
and  
Gregory D. Kutz  
Associate Director, Governmentwide Accounting  
and Financial Management Issues  
Accounting and Information Management Division



Statement

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## Debt Collection: Barring Delinquent Taxpayers From Receiving Federal Contracts and Loan Assistance

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Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to assist the Subcommittee in its consideration of H.R. 4181, a bill to amend Title 31, United States Code, to prohibit delinquent federal debtors, including delinquent taxpayers, from being eligible to contract with federal agencies. The bill would also generally preclude delinquent taxpayers from obtaining federal loans (other than disaster loans) or loan insurance or guarantees.

Our remarks today are based on the work we did at the request of the Subcommittee on unpaid payroll taxes and associated tax penalties and our past and ongoing audits of the Internal Revenue Service (IRS) and federal acquisition and loan assistance processes.

We support the concept of barring delinquent taxpayers from receiving federal contracts, loans, and loan guarantees and insurance. In fact, in 1992, we said Congress should consider whether tax compliance should be a prerequisite for receiving a federal contract.<sup>1</sup> However, with H.R. 4181, we believe there are significant implementation issues, particularly with respect to the federal acquisition process, and we offer recommendations for a phased-in implementation of the provisions and additional standards for when delinquent taxpayers should be barred. Our statement makes the following points:

- Taxpayers owe the federal government billions of dollars in delinquent taxes. For example, as we reported to this Subcommittee last August, as of September 30, 1998, nearly 2 million businesses owed \$49 billion in cumulative delinquent unpaid payroll taxes and 185,000 individuals responsible for the nonpayment of delinquent payroll taxes owed \$15 billion in trust fund recovery penalties (TFRP).<sup>2</sup> The majority of these unpaid payroll taxes and associated TFRPs are not likely to be collected for various reasons, including the delinquent taxpayers' inability or unwillingness to pay. A significant number of both businesses with delinquent unpaid payroll taxes and individuals with outstanding TFRPs also receive substantial payments from the federal government, either for

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<sup>1</sup>Tax Administration: Federal Contractor Tax Delinquencies and Status of the 1992 Tax Return Filing Season (GAO/T-GGD-92-23, Mar. 17, 1992).

<sup>2</sup>IRS assesses a TFRP against an individual, such as a corporate officer, who it determines was willful and responsible for not forwarding to the government the federal payroll taxes withheld from employees' salaries. The \$49 billion in cumulative unpaid payroll taxes includes about \$19 billion in unpaid tax assessments and another \$30 billion in penalties and interest. The \$15 billion in TFRPs include initial assessments of about \$9 billion and accumulated interest of about \$6 billion.

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federal benefits or loans or for other payment purposes, such as under federal contracts for goods and services.

- IRS currently does not have the systems that would enable it to consistently provide federal agencies with timely, accurate, and complete information on an individual's or business' tax delinquency status. IRS is undergoing a major systems modernization program, which will likely take several more years to complete. If these modernization efforts are successful, IRS may be able to provide agencies with timely, accurate, and complete tax delinquency status information that could be used as a basis for denying federal loan assistance and contracts to delinquent taxpayers.
- The Office of Management and Budget (OMB) currently directs administrators of federal loan, loan insurance, and loan guarantee programs to determine whether an applicant has any type of delinquent federal debt, including a tax debt, for the purpose of determining creditworthiness. However, in regard to tax debts, agencies may not always be complying with this directive. Moreover, because of IRS' systems limitations, prior to full implementation of H.R. 4181, a pilot test involving one or more federal loan assistance programs could help determine whether IRS' current systems can effectively and efficiently handle the volume of tax delinquency status requests that it would receive. The pilot could also help IRS develop and build into its modernization efforts the requirements for a real-time tax delinquency check program.
- In recent years, both Congress and the administration have attempted to streamline the government procurement system in an effort to reduce the cost of the system for both the government and its contractors. In large part, these efforts have involved eliminating administrative requirements not central to the fundamental purpose of the procurement system: purchasing best-value goods and services in an efficient, cost-effective manner. Unlike federal loan assistance programs, OMB does not direct federal agencies to check on a prospective contractor's tax debts. Thus, H.R. 4181 could add considerable burden to the acquisition process both in terms of costs and time. However, this burden could eventually be decreased if IRS' modernization efforts result in a system that gives contracting agencies an almost immediate response to their requests for information on the delinquency status of prospective contractors. To help reduce the burden on the acquisition process imposition of H.R. 4181's barring requirements on the acquisition process could be deferred until IRS has an effective and efficient tax delinquency check program.

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**Debt Collection: Barring Delinquent Taxpayers From Receiving Federal Contracts and Loan Assistance**

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- Generally, with the exception of taxpayers that have made arrangements with IRS to make payments on their tax debts, H.R. 4181 would deny loan assistance or contracts to all taxpayers with tax debts that have been outstanding for more than 90 days after the date the tax was assessed. As a starting point, the 90 days after assessment standard is not unreasonable. However, this provision may be too restrictive because it may not allow enough time for delinquent taxpayers to fully exercise their due process rights for settling their tax debts. Additionally, after 90 days from the date of the tax assessment, some taxpayers could still be in the process of negotiating payment agreements to resolve their delinquencies. To help ensure that taxpayers are not barred from receiving federal contracts or loan assistance while they are negotiating payment agreements, the Secretary of the Treasury could prescribe additional standards for IRS to use in determining when a person has a tax debt in delinquent status for purposes of barring under H.R. 4181.

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**H.R. 4181 Would Bar Delinquent Taxpayers From Obtaining Federal Loan Assistance or Contracts**

H.R. 4181 would amend the Debt Collection Improvement Act to extend to delinquent tax debtors the bar that currently prohibits the award of federal loans, loan guarantees, and loan insurance to nontax debtors whose debts are in delinquent status. The bill would also prevent an agency from entering into a contract with any "person" who owes a debt (nontax or tax) to a federal agency that is in delinquent status. The bill defines "person" to include a partnership with a partner who has been assessed a penalty for unpaid payroll taxes under section 6672<sup>2</sup> of the Internal Revenue Code of 1986. In addition, the definition of "person" includes a corporation with an officer or a shareholder who holds at least 25 percent of the outstanding shares of corporate stock who has been assessed a penalty under section 6672.

The bill specifically excludes from the barring provision any contract that is entered into for the performance of disaster relief as designated in standards prescribed by the Secretary of the Treasury and any contract designated by the President as necessary to the national security. Regarding tax debt, the bill establishes that, generally, unless the tax debt is being paid timely, the delinquent status commences 90 days after an assessment. The bill also requires that any agency administering a loan or loan guarantee program or requesting proposals for contracts require each loan applicant or prospective contractor to submit a form authorizing the Secretary of the Treasury to disclose to the agency whether the loan applicant or prospective contractor has a tax debt that has been outstanding for more than 90 days.

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<sup>2</sup>Section 6672 deals with TFRFs.

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### Delinquent Taxpayers Have Benefited From Federal Contracts and Loans

Our work at IRS over the past several years has shown that some taxpayers have benefited from federal loan and guarantee programs and have received federal contracts while they still had delinquent tax liabilities. In a disturbing number of instances, individuals have repeatedly failed to fulfill their tax obligations, starting up numerous businesses and then failing to pay their tax liabilities. In some cases, such individuals were actually assisted in this practice by obtaining federal loans or contracts. The barring provisions of the proposed bill would preclude individuals or businesses with all forms of delinquent tax debt from obtaining federal loans or contracts. H.R. 4181 would also attempt to preclude individuals responsible for the nonpayment of taxes owed by one business or partnership from obtaining federal loans or contracts for a second business or partnership.

As discussed in our report on unpaid payroll taxes,<sup>4</sup> according to IRS records, over 1.8 million businesses owed cumulative delinquent unpaid payroll taxes of about \$49 billion as of September 30, 1998. Nearly 50 percent of these businesses were delinquent for more than one tax period.<sup>5</sup> These businesses are typically in wage-based industries and are usually small, closely held businesses using a corporate structure, although this may vary. TFRPs totaling about \$15 billion were assessed against 185,000 individuals associated with these businesses. Our work showed that nearly 25,000, or about 13 percent of these individuals with penalty assessments, had been assessed such penalties for more than one business. About one quarter of these individuals were responsible for the nonpayment of payroll taxes at three or more businesses. The majority of these unpaid payroll taxes and associated TFRPs are not likely to be collected for various reasons, including the delinquent taxpayers' inability or unwillingness to pay.

We also found that, over a 3-month period, an estimated 16,700 civilian contractors who owed the federal government \$507 million in delinquent payroll taxes received about \$7 billion in federal payments.<sup>6</sup> Additionally, as of September 30, 1998, about 12,700 taxpayers (businesses and individuals), with delinquent payroll taxes totaling about \$295 million, had

<sup>4</sup>Unpaid Payroll Taxes: Billions in Delinquent Taxes and Penalty Assessments Are Owed (GAO/AMD/GGD-99-211, Aug. 2, 1999).

<sup>5</sup>For payroll taxes, the tax period is a quarter.

<sup>6</sup>There were several limitations related to this analysis. Owing to the sporadic nature of contract payments, we did not attempt to estimate an annual amount. These estimates are subject to estimation error and are based on unaudited data. In addition, serious deficiencies in IRS' financial management systems, such as the failure to timely post assessments, could cause an underestimation. Further, we did not include military contractors in our population of delinquent taxpayers.

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received Small Business Administration (SBA) loan disbursements totaling about \$3.5 billion.<sup>7</sup> Further analysis indicated that over 1,700 of these taxpayers received their SBA loans estimated at nearly \$449 million after they had accumulated unpaid payroll tax delinquencies of almost \$32 million.<sup>8</sup>

The general barring provisions are intended to end the contract award and lending practices that lead to delinquent taxpayers benefiting from federal business and programs. Other provisions of the bill seek to end the practice by some multiple tax offenders, who as corporate officers, employees, or partners, were assessed TFRPs, from using federal loans and contracts to start new businesses while the payroll taxes of other companies they were or are associated with remain unpaid. To the extent that any of the nearly 25,000 multiple tax offenders discussed earlier engage in this practice, the barring provisions of H.R. 4181 would attempt to preclude these individuals or their businesses, or any successor business or partnership that these individuals may be associated with, from obtaining additional federal contracts or loans.

Perhaps most importantly, the provisions of the proposed bill could serve as an incentive to individuals and businesses wishing to do business with the federal government to comply with their tax obligations, thus reducing the level of tax delinquencies and promoting compliance. This, in turn, would serve to provide fairness to compliant taxpayers who consistently fulfill their tax obligations, only to see a portion of their tax payments being used to finance federal loans and contracts to those who do not pay their fair share.

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**H.R. 4181 Poses  
Several  
Implementation Issues**

In considering this legislation, Congress should be aware of IRS' current inability to consistently provide federal agencies with timely, accurate, and complete information on loan assistance applicants' and prospective contractors' delinquency status. Congress may want to defer full implementation of H.R. 4181's barring requirements until there is assurance that IRS could make effective and efficient delinquency status checks.

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<sup>7</sup>For purposes of this study, we only looked at delinquent taxpayers receiving SBA loans. We did not broaden our work to search for delinquent taxpayers who received loans or guarantees through other federal lending programs.

<sup>8</sup>The attachment to our statement contains two examples from our detailed review of unpaid payroll tax case files of individuals and businesses that received some form of federal payment when they had multiple tax periods of unpaid payroll taxes.

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**IRS Does Not Have the Capability to Provide Accurate and Timely Delinquency Checks**

H.R. 4181 would require a system that provides accurate and complete information on loan assistance applicants' and prospective contractors' delinquency status on an almost instantaneous basis. IRS could potentially be required to annually verify the tax delinquency status of over one million loan assistance applicants and prospective contractors. However, as we reported in 1999 and again earlier this year,<sup>6</sup> IRS' systems are not currently capable of accessing and providing a complete and accurate status of a given taxpayer's account on a real-time basis. The lack of an automatic link or interface between IRS' business and individual master files prevents IRS from having a complete record of related taxpayer accounts to ensure that all activity, such as collections, are properly recorded in all related accounts. Without this information, IRS has no assurance that its records for an individual taxpayer or business are complete and accurate, and IRS would have to thoroughly analyze its records for a given taxpayer before ensuring that the account status is accurate. In our prior work, we found that IRS' system deficiencies have resulted in instances in which IRS has pursued and collected amounts that were no longer owed.

While IRS has made some progress in attempting to compensate for the lack of an automated interface between the two taxpayer databases, these efforts to date have not been fully effective in ensuring the accuracy of taxpayers' accounts. Until adequate automated systems are in place, it is not possible for IRS to ensure that only delinquent taxpayers that do not meet H.R. 4181 exemption provisions are barred from receiving a federal contract or loan assistance.

IRS recognizes that the age and complexity of its tape-based master file system, which holds critical taxpayer information, causes delays and inaccuracies in providing service to taxpayers. As a result, IRS is undergoing a major systems modernization effort to correct systems deficiencies. As part of this effort, it has a Customer Account Data Engine project to incrementally replace its old systems with new technology, new applications, and new databases.

According to IRS, the new system will allow employees to post transactions and update taxpayer account and return data from their desks. The updates are to be immediately available and provide a complete, timely, and accurate account of the taxpayer's information. The database and applications developed by the data engine project are to

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<sup>6</sup>GAO/AIMD/GGD-99-211, Aug. 2, 1999 and Financial Audit: IRS' Fiscal Year 1999 Financial Statement (GAO/AIMD-00-76, Feb. 29, 2000).

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enable the development of mission-critical modernization systems. IRS expects that these new systems will provide it with the capability to service taxpayers in a manner similar to that provided by commercial-sector financial service organizations. IRS expects to fully deploy the Customer Account Data Engine for individual taxpayers in 2005. Such a system for business taxpayers will not be available until after 2005.

The Customer Account Data Engine could allow IRS to have an effective and efficient tax delinquency status check system that should be able to provide federal agencies with immediate responses from IRS on a loan assistance applicant's or prospective contractor's tax delinquency status. In developing a tax delinquency status check system, IRS could use as a model the National Instant Criminal Background Check System used to make presale background checks for purchases from federal firearms licensees—about 72 percent of the criminal background checks result in approved responses within 30 seconds, while responses to most of the remaining 28 percent are provided within 2 hours or less.

**Loan Assistance Agencies  
Are Currently Directed to  
Check Applicants For  
Delinquent Taxes**

Agencies that administer loan, loan insurance, and loan guarantee programs are currently directed to determine whether an applicant has any type of delinquent federal debt, including a tax debt. Since 1993, OMB has directed agencies administering federal loan assistance programs to include on loan application forms a question asking applicants if they have a delinquent federal debt, including a tax debt, for the purpose of determining creditworthiness. Under OMB Circular A-129,<sup>10</sup> the agencies are to seek third-party assistance in determining whether applicants have federal debts and suspend processing applications when applicants have outstanding federal delinquencies. Processing may continue only after the debtor satisfactorily resolves the delinquency (e.g., pays in full or negotiates a repayment agreement). Similar to the Debt Collection Improvement Act of 1996, which codified OMB's bar on persons with nontax federal debts from receiving federal loan assistance, H.R. 4181 would codify the OMB guidance to bar persons with tax debts from receiving federal loan assistance.

Currently, under Internal Revenue Code section 6103(1)(3) an agency can contact IRS for information on an applicant's tax status to determine creditworthiness. We do not know how many federal loan assistance agencies contact IRS for this information, and when they do, whether they receive timely data that are accurate and complete. However, based on our prior unpaid payroll tax work, there are indications that agencies do not go

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<sup>10</sup> OMB Circular No. A-129, "Policies for Federal Credit Programs and Non-Tax Receivables."

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to IRS for delinquency information. For example, as we discussed earlier, over 1,700 taxpayers received SBA loans when they had payroll tax delinquencies.

Since agencies administering federal loan assistance programs already are directed to seek third-party assistance in determining whether an applicant has a federal debt, they should have time built into their application processes to make these determinations. Even so, before fully implementing the requirements of H.R. 4181, it would be prudent to conduct a pilot test of one or more loan assistance programs to determine whether IRS' current systems could effectively and efficiently handle the volume of delinquent requests that could be expected and what changes to its current processes and systems IRS would have to make. A pilot test would also be useful to IRS as it develops its new data systems to determine what capabilities would have to be incorporated in the new systems to handle the H.R. 4181 requirements.

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**H.R. 4181 Could Increase  
Federal Acquisition Cost**

Unlike its guidance for federal loan assistance programs, OMB does not direct federal agencies to check on the tax delinquency status of prospective contractors. Thus, H.R. 4181 could affect the federal acquisition process and impose an administrative burden on agencies and on those wishing to do business with the government. We believe that efforts to address delinquent federal debt must be cost-effective. In this regard, the provision in the bill that would bar the award of federal contracts to those with delinquent federal debts might not meet this test. In recent years, both Congress and the administration have attempted to streamline the government procurement system in an effort to reduce the cost of the system for both the government and its contractors. In large part, these efforts have involved eliminating administrative requirements not central to the fundamental purpose of the procurement system: purchasing best-value goods and services in an efficient, cost-effective manner.

We do not know the extent of all of the costs, in terms of time and resources, that H.R. 4181 requirements may impose on the acquisition process and prospective customers. However, with regard to costs associated with the time it takes to award contracts, these could be reduced if IRS' modernization efforts result in a system that would give contracting agencies an almost immediate response to their requests for information on the delinquency status of prospective contractors. Since federal agencies are not currently required to deny awards based on prospective contractors' tax debts, the appropriate time to impose H.R.

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4181 requirements on the acquisition process may be after IRS has the capability to effectively and efficiently check tax delinquencies.

In the meantime, beginning in July 2000, federal civilian contractors who have tax debts are to be subject to a program under which IRS can levy a portion of their contract payments. Provisions in the Taxpayer Relief Act of 1997 gave IRS authority to levy up to 15 percent of certain federal payments made to delinquent taxpayers. The payments include federal civilian agency vendor payments, Social Security benefits, and federal salary and retirement payments. When this continuous levy program is operational, IRS will be able to electronically serve tax levies on vendor payments made through the Department of the Treasury's Financial Management Service (FMS). Federal loan assistance payments are not subject to this levy program.

While the levy program will not prevent delinquent contractors from receiving federal contracts, it may allow IRS to collect delinquent taxes from some of the contractors who owe them. Our review of the continuous levy program showed that of 761,000 taxpayers that received federal vendor payments in the first quarter of 1999, about one percent, or 7,600 vendors, had delinquent taxes that would have been subject to the continuous levy program if it were operational.<sup>11</sup> The 7,600 vendors had \$362 million in delinquent taxes and received federal vendor payments totaling about \$2 billion. We estimated that about \$104 million of the vendor payments could be levied annually.

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**The 90-Day Barring Requirement May Be Too Restrictive**

Generally, with the exception of taxpayers that have entered into agreements with IRS to pay off their tax debts, H.R. 4181 would deny loans or contracts to all taxpayers that have a tax debt more than 90 days after the date the tax was assessed. The 90-day barring requirement may prevent taxpayers that are still attempting to reach agreement with IRS regarding their tax debts from receiving federal loans or contracts.

IRS has for years had a graduated collection process that generally consisted of, first, sending delinquent taxpayers a series of notices over a period of 11 to 21 weeks before attempting personal contact through telephone calls or in-person visits.<sup>12</sup> If after these personal contacts IRS

<sup>11</sup>Tax Administration: IRS' Levy of Federal Payments Could Generate Millions of Dollars (GAO/GGD-00-65, Apr. 7, 2000). Delinquent vendors not subject to the continuous levy program include those who were paying off their tax debts or who IRS has determined do not currently have the financial resources to pay down their tax debts.

<sup>12</sup>After a tax assessment is posted to IRS records and the tax has not been paid, IRS sends taxpayers a series of balance-due notices. The first notice is to be sent within a week or so after the tax assessment.

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**Statement**  
**Debt Collection: Barring Delinquent Taxpayers From Receiving Federal Contracts and Loan Assistance**

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cannot settle the delinquent account, it can initiate enforced collection actions to collect the delinquent tax, such as by levying taxpayers' bank accounts or seizing their assets.

The IRS Restructuring and Reform Act of 1998 provided taxpayers with additional rights and protections before IRS could take enforced collection action, which further lengthened the collection process. The Restructuring Act required IRS to provide taxpayers with additional notifications of its intent to take enforced collection actions and expanded taxpayer rights to appeal such decisions. For example, the Restructuring Act required that IRS give the taxpayer written notice within 5 business days after filing a lien and an additional 30 days before initiating a levy or seizure action.

The 90-day timeframe for deeming a tax debt delinquent could coincide with certain collection tools IRS currently uses to seek compliance. For example, many delinquent taxpayers apply for offers-in-compromise<sup>13</sup> to settle their tax debt. These applications are usually made later than 90 days from the date the tax was assessed. Even if an application were made within the 90-day period, H.R. 4181 would bar the individual from receiving a loan or contract because of the time it takes IRS to process offer applications. IRS' own performance measure for processing offers is the percent of offers closed within 6 months of the date the offer application is accepted for investigation. For fiscal year 1999, IRS met this goal for only 51 percent of its cases.

One way to help ensure that taxpayers are not barred from receiving federal contracts or loans while they are negotiating a payment agreement would be to require the Secretary of the Treasury to prescribe additional standards for IRS to use in determining whether a person has an outstanding tax debt that would be subject to H.R. 4181's barring requirements. A similar approach was taken in the Debt Collection Improvement Act of 1996 in regards to nontax federal debts. This act required the Secretary of the Treasury to prescribe standards under which agencies would determine whether a person had an outstanding delinquent debt that would trigger the Debt Collection Act's bar on federal loan assistance.

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<sup>13</sup> is posted. For individual taxpayers, IRS can send up to three additional notices at 5-week intervals. About 6 weeks after the fourth notice is sent, IRS attempts to make personal contact with taxpayers. The notice process is shorter for businesses. Five weeks after the initial notice, IRS is to send a second notice and wait 6 weeks after this notice before attempting personal contact.

<sup>14</sup> An offer-in-compromise is a taxpayer proposal to settle a tax debt for less than the amount owed.

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Statement  
Debt Collection: Barring Delinquent Taxpayers From Receiving Federal Contracts and Loan Assistance

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## Conclusions and Recommendations

We support the concept of barring delinquent taxpayers from receiving federal contracts, loans, and loan guarantees and insurance. Our work has shown that some delinquent taxpayers receive billions of dollars in federal contract payments, loans, and other federal benefits. H.R. 4181 would prevent most of these delinquent taxpayers from receiving additional loans, loan guarantees, loan insurance, or contracts until they pay off their delinquent tax debts or enter into agreements with IRS to pay off their tax debts. This bill would provide a measure of fairness to the vast majority of taxpayers who consistently fulfill their tax obligations, only to see a portion of their tax payments being used to finance federal loans and contracts to those who do not pay their fair share.

However, as we have explained, this bill presents several significant implementation issues. As we have reported for years, IRS' systems are unable to provide timely and accurate data on taxpayer accounts. For this reason and because the impact on IRS' systems of the potentially large volume of requests for delinquency status information is unknown, we recommend that Congress provide that the H.R. 4181 requirements be implemented initially on a pilot basis for loans, loan guarantees, and loan insurance. With respect to federal contracts, we recommend that Congress defer the application of the barring provisions of H.R. 4181 until the results of the pilot program for loan assistance and the success of IRS' systems modernization are known. We believe that application of H.R. 4181 barring requirement to the federal acquisition process at this time could unduly delay the procurement of needed goods and services to the federal government and increase the cost of the federal acquisition process. We could support the application of H.R. 4181 to the federal acquisition process only after IRS is able to determine in a matter of hours whether prospective federal contractors have delinquent tax debt.

The 90-day provision in H.R. 4181 for determining when a tax debt meets the barring requirement may be too restrictive because it may not allow enough time for delinquent taxpayers to fully exercise their due process rights for collection actions or to negotiate payment agreements with IRS to settle their tax debts. To help ensure that taxpayers are not prematurely barred from receiving federal contracts or loan assistance, we recommend that Congress require the Secretary of the Treasury to prescribe additional standards for IRS to use in determining when a taxpayer has an outstanding tax debt in delinquent status for purposes of barring under H.R. 4181.

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Mr. Chairman, this concludes my statement. We welcome any questions that you may have.

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**Statement**  
**Debt Collection: Barring Delinquent Taxpayers From Receiving Federal Contracts and Loan Assistance**

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**Contact and Acknowledgements**

For further contacts regarding this testimony, please contact Cornelia M. Ashby at (202) 512-9110 or Gregory D. Kutz at (202) 512-3406. Individuals making key contributions to this testimony included Thomas Armstrong, Ralph Block, Shirley Jones, Franklin Jackson, Andrea Levine, and Steven Sebastian.

Attachment

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## Examples of Unpaid Payroll Tax Delinquency Cases

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The issues pertaining to individuals and businesses with multiple tax periods of unpaid payroll taxes receiving federal loans and contracts can be illustrated by two specific examples from our detailed review of unpaid payroll tax case files. It is important to note that these are just two of numerous examples of such occurrences we have observed in our work at IRS over the past several years. In each of these cases, the IRS files provided evidence of the businesses or individuals responsible for delinquent federal taxes having diverted monies for senior management's benefit or received federal payments (e.g., loans, contracts) or a combination of the two. In the first case, HR 4181 would attempt to preclude individuals who form new companies and were responsible for the nonpayment of payroll taxes from getting federal loans or guarantees, or from getting federal contracts. In the second case, if the company had applied for its SBA loan subsequent to becoming delinquent on its first quarter of payroll taxes, the provisions of HR 4181 would have prevented this business from obtaining the SBA loan.

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### Case 1

The first case involved a company that operated as a freight handler and had agreements with the U.S. Navy and other federal agencies. In fact, in 1993, federal government agreements accounted for 85 percent of the company's revenues, and in 1994, accounted for 65 percent of company revenues. In early 1995, an accounting firm retained by the company's officers reported an estimated \$2 million unpaid payroll tax liability and related tax returns (form 941s) that had not been filed with the IRS for the last two quarters. Officers of the company initially interviewed by IRS claimed to have no idea why funds associated with the payroll tax liabilities had not been remitted to IRS and accused the former controller of being responsible. However, IRS determined that the former controller did not have the ability to exercise control over financial matters, did not have check-signing authority, and was not a corporate officer.

Further investigation by IRS revealed that corporate funds were routinely funneled to another company owned by one of the officers and, in turn, used to acquire trucks, equipment, and an expansion of terminal locations on the East Coast. The company's corporate tax return for 1994 showed that, during the period in which the company's payroll taxes went unpaid, over \$2 million was advanced to the affiliated company. At the same time, the company's bank account balances showed that there were adequate funds to meet the payroll tax obligations. IRS determined that the primary corporate officer who owned the affiliated company had full signature authority, directed the payment of all bills, and retained authority over all financial matters.

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Attachment  
Examples of Unpaid Payroll Tax Delinquency Cases

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Ultimately, IRS determined that funds for unpaid payroll taxes were also being used for corporate officers' personal expenses, including:

- Paying the estimated taxes of corporate officers,
- Installing and maintaining a swimming pool for the primary officer,
- Paying off a personal car loan for the primary officer's wife,
- Purchasing a tractor for home use, and
- Storing and maintaining at least eight antique cars owned by the primary officer.

The company eventually filed for bankruptcy. Additionally, IRS has determined that the payroll taxes of the primary officer's other company have also not been paid, and at the time we completed our work, there was a substantial tax delinquency for this company.

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Case 2

The second case involved a garment manufacturing company, with outstanding federal loans and delinquent payroll taxes at the time of our review, which has since gone out of business. The company began experiencing cash flow problems almost from its inception in 1980, and it had delinquent payroll taxes for six quarters between 1981 and its last year of operation, 1988. At the time it went bankrupt, the business had an outstanding SBA loan. No trust fund recovery penalties had been assessed against the company's officers, despite evidence that the company president (who also served as vice president and treasurer) used funds to pay other creditors in an attempt to keep the business from folding. The president, while not assessed a penalty for the delinquent payroll taxes associated with this business, had been assessed penalties for delinquent payroll taxes for two other businesses in which he was involved.

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Mr. HORN. Our next presenter is Deidre Lee, the Acting Deputy Director for Management, Office of Management and Budget. Nice to have you here again.

Ms. LEE. Good morning. Chairman Horn, Congressman Turner, and members of the subcommittee, I have been asked to discuss the administration's views on H.R. 4181, the Debt Payment Incentive Act of 2000. The bill would amend Title 31 of the U.S. Code to bar delinquent debtors from obtaining Federal contracts. It also adds delinquent debt as a bar to obtaining not only Federal contracts but other types of Federal assistance.

The administration shares the subcommittee's goal to reduce delinquency. We supported the Debt Collection Improvement Act of 1996 which provided a comprehensive set of tools for agencies to use at their discretion to improve account servicing and debt collection, such as consolidating and cross servicing the Treasury offset program and loan sales assets. The tools have allowed us to reduce our delinquent nontax debt from \$60 billion in fiscal year 1998 to \$53 billion in 1999, and we expect a continued decline as agencies sell delinquent loan assets to the private sector and refer greater amounts of delinquent debt to Treasury for cross servicing, but this is not enough. We need to continue to reduce that debt.

We have supported H.R. 436, Government Waste, Fraud, and Error Reduction Act of 1999, which would have strengthened the provisions of the Debt Collection Improvement Act, including barring delinquent nontax debtors from receiving Federal benefits.

In support of these legislative efforts, the President has declared improved management of Federal receivables to be a priority management objective. Priority management objections are OMB's highest management priorities for the Federal Government. These objectives are areas in need of reform and receive ongoing attention from the administration in the most senior levels of OMB and the agencies.

Notwithstanding our support for improved debt collection, we are concerned that the bill, without modification, may undo some of the important progress this committee has helped us to achieve in reforming the procurement process.

I would like to highlight for you how H.R. 4181 would affect the procurement process, some concerns we have with certain provisions, and some suggestions that we would like to offer. I will defer to the Department of Treasury on the implementation of their aspects of the bill.

As you know, an efficient, economical, and well functioning procurement system requires the award of contracts to individuals and organizations that meet high standards of integrity and business ethics. The government should only be doing business with high performing and successful companies that work to maintain a good record of compliance with their responsibilities as entities within the community. At the same time, we have been striving in recent years to ensure that our procurement tools provide the flexibility to acquire those goods and services necessary to carry out the mission of the agency in an efficient and expeditious manner.

As we work together to strengthen our debt collection efforts, we also need to preserve the achievements of our recent procurement reform efforts. The ability of the contracting officer to exercise good

business judgment in their contracting decisions has been critical to procurement reform. The bill provides exceptions for national security and disaster relief but there may be other circumstances where exceptions should apply.

For example, the bill could provide contracting officers with the discretion to assess on a case by case basis whether a delinquent debtor should be barred from Federal contracting.

I am also concerned that the lack of contracting officer discretion may have adverse impact on small business. As you know, many small businesses need the constant cash-flow, and we need to balance the ongoing contracts they have in the offset and collection procedures and perhaps evaluate how that would impact them.

I would also suggest a dollar threshold. As Mr. Turner mentioned, we have a large number of small dollar activities that from timeframe and sheer volume we should look at their impact and how these could be assessed.

The simplified acquisition procedure of \$100,000 might be a threshold to consider.

This bill requires verification of not only corporate debtor status but also the status of officers and major shareholders who have been assessed a penalty for failure to collect and account for payroll taxes. This means that the contracting officer will have to check the delinquent status of not only the corporation but the officers and major shareholders, and similarly this will affect partnerships that have many partners. So our concern here, again, and I think it has been mentioned by others, is how do we set up that system to ensure that we can check this large number of individuals and do that on a fairly quick turnaround to provide the information.

The bill defines a delinquent tax debt as a debt that is not paid within 90 days, and as already addressed by Ms. Ashby, we think there are some definitional issues that could be straightened out or clarified here. For example, someone may be in recovery status and they are still delinquent but they are recovering that debt. How do we address that in this bill?

In light of these concerns, careful consideration should be given to strengthening the current mechanisms for dealing with delinquent debtors. For example, pursuant to the Debt Collection Improvement Act, the Treasury Department maintains an offset program to collect nontax debt. Under this program contract payments owed by a Federal contractor may be used to offset debts the contractor owes to the Federal Government. Federal agencies routinely report their contractor's taxpayer identification number to the IRS when contracts are awarded so that the IRS is aware of the companies with whom Federal agencies do business.

This process enables the IRS to issue tax levies if a contractor has an unpaid debt. Under this process, amounts otherwise paid to the contractor are paid to the IRS to offset the tax debt. An alternative to the bill under consideration might be to expand or improve these programs.

Notwithstanding the final language of the bill, again as Ms. Ashby stated, we should include a provision that would allow time to make sure the verification system is in place and then, of course, in addition to that there are some considerations on how we put

into place the Federal acquisition guidelines to explain to the contracting officers and the contractors how this process will operate.

Like this committee, the administration strongly supports collection of debts owed to the government. We met recently last week with your staff to discuss several of the issues that I have discussed today, and we would be glad to continue that dialog.

I hope we can work together to formulate a proposal with the goals that we can both share, and reduce the delinquent debt. This concludes my formal remarks and I would be happy to answer any questions.

Mr. HORN. Thank you very much.

[The prepared statement of Ms. Lee follows:]



EXECUTIVE OFFICE OF THE PRESIDENT  
OFFICE OF MANAGEMENT AND BUDGET  
WASHINGTON, D.C. 20503

TESTIMONY OF  
DEIDRE A. LEE

ACTING DEPUTY DIRECTOR FOR MANAGEMENT  
OFFICE OF MANAGEMENT AND BUDGET

BEFORE THE

HOUSE COMMITTEE ON GOVERNMENT REFORM

SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION AND TECHNOLOGY

ON H.R. 4181, DEBT PAYMENT INCENTIVE ACT OF 2000

MAY 9, 2000

Chairman Horn, Congressman Turner, and members of the Subcommittee, I have been asked to discuss the Administration's views on H.R. 4181, the "Debt Payment Incentive Act of 2000." This bill would amend Section 3720B of Title 31 of the U.S. Code to bar delinquent debtors from obtaining Federal contracts. It also adds delinquent debt as a bar to obtaining, not only Federal contracts, but to other types of Federal assistance.

PROGRESS ON DEBT COLLECTION TO DATE

The Administration shares the Subcommittee's desire to reduce debt delinquency. We supported the Debt Collection Improvement Act of 1996 (DCIA), which provided a comprehensive set of tools for agencies to use at their discretion to improve account servicing and debt collection, such as consolidated cross-servicing, the Treasury Offset Program (TOP) and loan asset sales. The tools have allowed us to reduce our delinquent non-tax debt from \$60

billion in FY 1998 to \$53 billion in FY 1999, and we expect a continued decline as agencies sell delinquent loan assets to the private sector and refer greater amounts of delinquent debt to Treasury for cross-servicing. We also supported H.R. 436, Government Waste, Fraud, and Error Reduction Act of 1999, which would have strengthened the provisions of the DCIA, including barring delinquent non-tax debtors from receiving Federal benefits. In support of these legislative efforts, the President has declared improved management of Federal receivables to be a Priority Management Objective. PMOs are OMB's highest management priorities for the Federal government. These objectives are areas in need of reform, and receive ongoing attention from the Administration and the most senior levels of OMB.

Notwithstanding our support for improved debt collection, we are concerned that the bill, without modification, may undo some of the important progress this Committee has helped us to achieve in reforming our procurement process. I would like to highlight for you how H.R. 4181 would affect the procurement process; some concerns we have with certain provisions; and some suggestions that we would like to offer. I will defer to the Department of the Treasury on the implementation of their aspects of the bill.

An efficient, economical and well-functioning procurement system requires the award of contracts to individuals and organizations that meet high standards of integrity and business ethics. The government should only be doing business with high-performing and successful companies that work to maintain a good record of compliance with their responsibilities as entities within the community. At the same time we have been striving in recent years to ensure that our procurement tools provide the flexibility to acquire those goods and services necessary to carry out their mission in an efficient and expeditious manner.

## ISSUES AND RECOMMENDATIONS

The ability of the contracting officer to be flexible has been critical to procurement reform. The bill provides exceptions for national security and disaster relief, but there may be other circumstances where exceptions should apply. For example, the bill could provide contracting officers with the discretion to assess whether a delinquent debtor should be barred from Federal contracting.

I am concerned about the impact on small businesses. Cash flow is an everyday problem for all businesses and especially small businesses. While large businesses have plentiful lines of credit, small businesses do not have the same access. Discretion for the contracting officer might ameliorate this impact.

I would also suggest a dollar threshold. The bill applies to all Federal contracts without regard to size. One option would be to exempt acquisitions below the simplified acquisition threshold, which is \$100,000.

The bill requires verification of not only corporate debtor status, but also the status of its officers and major shareholders who have been assessed a penalty for failure to collect and account for payroll taxes. This means that the contracting officer will need to check the delinquent status of not only the corporation but also its officers and major shareholders before awarding the contract and develop systems for doing so. Similarly, partnerships would be held responsible for all partners in a firm which could number hundreds of people in some case. A method for verification would need to be developed with the capability to provide this information to the contracting officer in an expeditious manner.

The bill defines a delinquent tax debt as a debt that has not been paid within 90 days of an

assessment of a tax, penalty, or interest under the Internal Revenue Code of 1986. It is not clear that this definition would provide adequate due process for contractors, or how disputed debts would be treated under this standard. In this regard, the testimony from the Department of the Treasury offers some suggestions on how to refine the definition.

#### ALTERNATIVES

In light of these concerns, careful consideration should be given to strengthening current mechanisms for dealing with delinquent debtors. For example, pursuant to DCIA, the Treasury Department maintains an offset program to collect non-tax debt. Under this program, contract payments owed to a Federal contractor may be used to offset debts the contractor owes to the Federal government. Federal agencies routinely report their contractors' taxpayer identification numbers to the Internal Revenue Service when contracts are awarded so that the IRS is aware of the companies with whom Federal agencies do business. This process enables the IRS to issue tax levies if a contractor has an unpaid tax debt. Under this process, amounts that would otherwise be paid to the contractor are paid to the IRS to offset the tax debt. An alternative to the Bill under consideration might be to expand or improve these programs.

Notwithstanding the final language of the bill, the committee should include a provision that allows an adequate amount of time to establish a verification system and publish guidance to the contracting officer through the Federal Acquisition Regulation.

CONCLUSION

Like this committee, the Administration strongly supports efforts to collect on debts owed to the government. However, there are several issues that need to be addressed to make this proposal into a workable solution. We met with committee staff this past week to discuss several of the issues I have identified today, and we would be glad to continue that dialogue. I would hope that we could work together to fashion a proposal that can advance the goals we both share.

This concludes my formal remarks. I am available to answer any questions you may have regarding my comments.

Mr. HORN. Our next presenter is Joe Mikrut, the Tax Legislative Counsel for the Department of the Treasury.

Mr. MIKRUT. Thank you, Mr. Chairman.

Mr. Chairman, Ranking Member Turner, distinguished members of the subcommittee, good morning. I appreciate the opportunity today to discuss with you the Federal tax policy aspects of the provisions of H.R. 4181, the Debt Payment Incentive Act of 2000. Section 3720(b) of Title 31 the U.S. Code enacted as part of the Debt Collection Improvement Act of 1996 currently bars a person from obtaining loans, loan guarantees, or loan insurance administered by a Federal agency if the person has an outstanding Federal debt other than a tax debt that is in delinquent status.

H.R. 4181 would amend section 3720(b) in two key aspects. First, it would extend the act to persons applying for Federal contracts. Second, it would extend the act to tax debts as well as nontax debts.

Treasury supports efforts to reduce delinquent debt, both tax debt and nontax debt. To effectively achieve this result, however, a number of policy and technical issues must be addressed.

The two primary policy issues deal with the effects on voluntary tax compliance and the effects on taxpayer privacy rights.

The more general tax policy issue raised by the bill that must be considered is its effect on voluntary tax compliance. Ours is a system of voluntary tax compliance dependent upon self-assessment. We rely upon taxpayers to personally determine or assess their tax liabilities, to file tax returns, and to timely remit any taxes owed. The role of the IRS is to facilitate, monitor, and enforce this process. Anytime a person's tax status becomes relevant for nontax purposes, an incentive is created to misreport or, in some cases, to fail to report a tax liability in order to obtain this other benefit.

Because it takes longer for a taxpayer who does not file a tax return to be reflected as delinquent in the IRS records, the bill could have the potential effect of encouraging people not to file returns to avoid detection. On the other hand, the bill could have the opposite effect on enhancing tax compliance by encouraging taxpayers to avoid tax delinquent status by either paying their tax debts or pursuing other appropriate procedural avenues.

The second important policy consideration that the bill deals with is with respect to taxpayer privacy. In general, in order to encourage tax compliance, current law makes private a taxpayer's confidential tax information. Current law contains certain exceptions to this rule. H.R. 4181, by necessity, would require a disclosure of taxpayer information, that is, the taxpayer's delinquency status, to administering Federal agencies. We have some suggestions on how to best achieve the conflicting goals of taxpayer privacy and the need for information under the bill.

Under the bill, in connection with the loan application or a contract proposal, taxpayers would be required to authorize the Secretary of the Treasury to disclose whether they had a debt under the Internal Revenue Code that is in delinquent status. Treasury would be required to develop a form for such purposes. The authority for such disclosure would be under section 6103 of the Code which permits the disclosure of returns or return information upon consent.

Treasury recommends that the disclosures contemplated by the bill should be made, instead, by amending section 6103(l)(3), which currently provides explicit statutory authority for similar types of disclosures without the taxpayer's consent. This is consistent with the statutory scheme of 6103, generally, under which large scale disclosures, as contemplated by the bill, typically are achieved through an explicit statutory exception that grants an agency automatic access to return information.

In addition, different rules and procedures apply to disclosures pursuant to 6103(c) than are pursuant to explicit statutory exceptions. Explicit statutory exceptions typically specify exactly which information can be disclosed, to whom and for what purposes.

In addition, many of the disclosures are subject to special record-keeping and safeguarding procedures. Disclosures pursuant to consent under 6103(c), by contrast, have none of these limitations.

Finally, while statutory disclosures are typically at least partly automated, 6103(c) waivers typically involve a paper process and are subject to review for compliance with certain regulatory requirements by the IRS.

Currently, about 2 million third party consents are processed each year by the IRS. The disclosures required by this bill would add substantially to that number and would be difficult to administer and thus create delays in granting loans and contracts.

Another important consideration relevant to disclosure of return information under this provision is that many Federal agencies use contracts to administer their programs. The Congress traditionally has restricted access to return information by contractors even when disclosure otherwise may have been authorized due to concerns about taxpayer privacy.

In order to protect taxpayer privacy, the amendment to section 6103(l)(3) should make explicit that disclosures to contractors of the agencies administering the loans or entering into contracts will be permitted for purposes only of this provision, subject to the contractor's agreement to otherwise maintain the confidentiality of information, and subject to the agency's demonstrated oversight of the contractor's compliance with these safeguards.

We certainly recognize the value of notice provided by requiring taxpayers to authorize the necessary disclosures. We suggest that such notice should be incorporated into the loan application process or the contracting process without each notice having the legal effect of authorizing disclosure as would happen under section 6103(c) consent.

In addition to concerns about the effects of voluntary tax compliance and taxpayer privacy, we have certain technical comments on the bill. The most fundamental is the definition of tax delinquency. The bill currently defines tax delinquent status to be any Federal tax debt that has not been paid within 90 days of assessment.

Treasury recommends modification or deletion of this provision. The language may be unnecessary in light of section 3720(B)(a) which grants Treasury the authority to define delinquent status. Alternatively, we believe that the bill should make it explicit that a debt will not be considered to be in tax delinquent status if the taxpayer has either already administratively or judicially appealed

or still has the opportunity to administratively or judicially appeal a determination of the IRS.

This is generally consistent with the approach of 3720(B). It should be noted, however, that it can take a significant amount of time for a taxpayer to exhaust all its administrative and judicial remedies with respect to a Federal tax debt.

In any case, Treasury should have the authority and the flexibility to determine additional standards for consideration of a tax debt to be in delinquent status. For example, it might be appropriate to exclude delinquencies of nominal amounts.

Regardless of how precisely a tax delinquent account is defined, significant procedural and systems changes would be necessary for the IRS to be able to track, analyze, and communicate the information necessary to implement the provisions of the bill.

At least initially the process would involve labor intensive analysis of each relevant taxpayer's account. The IRS preliminarily estimates that the procedural changes could take at least 18 months to implement. Automation of this process, if possible, would require significant systems changes on top of the IRS' already planned modernization efforts and could be years off.

We have had additionally suggested technical modifications to the bill which we have shared with the majority and with minority staffs and we look forward to working with the subcommittee in developing these proposals.

In general, Mr. Chairman, in light of Treasury's policy and technical concerns with the bill, we suggest that, if it were enacted, you give careful consideration to the GAO's recommendation that it be initiated as a pilot program or some similar form. This would permit an overall evaluation of the effectiveness of the program, including its effect on tax compliance, and would provide the IRS with an opportunity to develop procedures or the systems necessary to implement this program.

This concludes my prepared remarks. We look forward to working with the Congress in addressing these concerns as the legislation develops, and I would be happy to respond to your questions.

Mr. HORN. Those are very helpful comments and we appreciate that.

[The prepared statement of Mr. Mikrut follows:]

**EMBARGOED UNTIL 10:00 A.M. EDT**

Text as Prepared for Delivery

May 9, 2000

**TAX LEGISLATIVE COUNSEL JOSEPH MIKRUT TESTIMONY  
BEFORE THE HOUSE SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION AND TECHNOLOGY**

Mr. Chairman, Ranking Member Turner, and distinguished Members of the Subcommittee:

I appreciate the opportunity to discuss with you today the provisions of H.R. 4181, the "Debt Payment Incentive Act of 2000."

**Description of Current Law**

Section 3720B of Title 31 of the United States Code (enacted as part of the Debt Collection Improvement Act of 1996) currently bars a person from obtaining loans, loan insurance, or loan guarantees administered by a Federal agency if the person has an outstanding debt, other than a debt under the Internal Revenue Code of 1986, with any Federal agency that is in delinquent status. This provision can be waived by the head of the Federal agency administering the loan program.

Section 6103(l)(3) of Title 26 of the United States Code (the Internal Revenue Code of 1986) provides that upon written request by the head of a Federal agency administering a Federal loan program, the Secretary of the Treasury may disclose whether or not a loan applicant has a tax delinquent account. Disclosures under this section may be made only for purposes of, and to the extent necessary in, determining the creditworthiness of the applicant.

**Description of the Bill**

H.R. 4181 would amend section 3720B in two key respects. First, it would extend the provision to persons applying for Federal contracts. Second, it would extend the provision to tax debts as well as nontax debts. For the latter purpose, the bill provides that each loan applicant or prospective Federal contractor would be required to sign a form authorizing the Secretary of the Treasury to disclose to the head of the Federal agency information describing whether the loan applicant or prospective contractor had an outstanding tax debt in delinquent status.

LS-612

### Treasury's Comments on Specific Aspects of the Bill

Treasury generally supports efforts to reduce delinquent debt, both tax and nontax. To effectively achieve this result, however, a number of policy and technical issues must be addressed.

#### Effect on Voluntary Tax Compliance

The most general tax policy issue raised by the bill that must be considered is its effect on voluntary tax compliance. Ours is a system of voluntary tax compliance dependent upon self-assessment. Anytime a person's tax status becomes relevant for nontax purposes, an incentive is created to misreport – or not report at all -- tax liability in order to obtain another benefit or to avoid another obligation. Indeed, because it takes longer for a taxpayer who does not file a return to be reflected as delinquent in IRS records, this provision could have the effect of encouraging people not to file returns. Similarly, taxpayers might be encouraged to file frivolous lawsuits in order to avoid delinquent status. On the other hand, the provision could have the effect of enhancing tax compliance by encouraging taxpayers to avoid tax delinquent status by either paying their tax debts or pursuing other appropriate procedural avenues.

#### Definitional and Operational Issues With Respect to "Tax Delinquent Accounts"

The issue of how to define tax delinquent status takes on greater significance under the bill than currently exists for purposes of section 6103(l)(3) because the determination of tax delinquent status under the bill would result in an automatic denial of loans or contracts, a potentially harsher result than merely factoring such status into a determination of creditworthiness as is currently the case under section 6103(l)(3). The bill currently defines tax delinquent status to be any Federal tax debt that has not been paid within 90 days of assessment. Treasury recommends that this provision be deleted. This language is unnecessary in light of section 3720B(a), which grants Treasury the authority to define delinquent status. Alternatively, Treasury believes that the bill should make it explicit that a debt will not be considered to be in tax delinquent status if the taxpayer has either already administratively or judicially appealed or is in the process of administratively or judicially appealing a determination by the Internal Revenue Service (IRS). This is consistent with the approach taken with respect to nontax debts in the existing regulations under section 3720B (31 C.F.R. §285.13). It should be noted, however, that it can take a significant amount of time for a taxpayer to exhaust all administrative and judicial remedies with respect to a Federal tax debt. In either case, Treasury should have the authority and flexibility to determine additional standards for considering a tax debt to be in delinquent status. For example, it may be appropriate to exclude delinquencies of nominal amounts.

In addition, in certain circumstances, taxpayers may be provided opportunities to contest the underlying tax liabilities *after* assessment. For example, the IRS Restructuring and Reform Act of 1998 provides additional due process safeguards for innocent spouses and taxpayers subject to collection procedures. To ensure that taxpayers in these and other situations are not considered delinquent, Treasury believes the bill and/or implementing regulations also should clarify that a tax debt would not be considered to be in delinquent status if the taxpayer has not

been provided the opportunity to contest the underlying liability before the IRS Office of Appeals.

Regardless of precisely how a tax delinquent account is defined, significant procedural and systems changes would be necessary for the IRS to be able to track, analyze, and communicate the information necessary to implement the provisions of the bill. At least initially, the process would involve labor-intensive analysis of each relevant taxpayer's account. IRS estimates that procedural changes could take at least eighteen months to implement. Automation of this process, if possible, would require significant systems changes on top of IRS's planned modernization efforts and would be years off.

#### **Provisions Relating to Responsible Person Penalties for Trust Fund Taxes**

Under the bill, a person would be defined, in the case of a corporation, as any corporation with a shareholder owning at least 25 percent of the shares of stock in that corporation and who has been assessed a penalty under section 6672. This is intended to prevent avoidance of this provision by reincorporating a business that had been subject to the penalty. However, in the case of a partnership, a section 6672 penalty of any partner would subject the partnership to this provision. We recommend that this provision similarly be limited to partners with at least a 25 percent interest in the partnership. Otherwise the provision potentially will be unfair to large partnerships and difficult to administer. We note that in both cases, IRS does not currently collect information necessary for determining 25 percent ownership. We suggest that partnerships and corporations applying for Federal loans or contracts should be required to provide a list of such partners or shareholders under penalties of perjury.

#### **Disclosure Provision**

Under the bill, in connection with loan applications or contract proposals, taxpayers would be required to authorize the Secretary of the Treasury to disclose whether they had a debt under the Internal Revenue Code of 1986 in delinquent status. Treasury would be required to develop a form for such purpose. The authority for such a disclosure would be section 6103(c) of the Internal Revenue Code, which permits the disclosure of returns or return information to persons designated by the taxpayer.

Treasury recommends that the disclosures contemplated by the bill should instead be made via an amendment to section 6103(l)(3), which currently provides explicit statutory authority for similar types of disclosures without the taxpayer's consent. This is consistent with the statutory scheme of section 6103 generally, under which large-scale disclosures typically are achieved through an explicit statutory exception to section 6103 that grants an agency automatic access to returns or return information for specific purposes. In addition, different rules and procedures apply to disclosures pursuant to section 6103(c) than apply to disclosures pursuant to explicit statutory exceptions. Explicit statutory exceptions typically specify exactly which information can be disclosed, to whom, and for what purposes. In addition, many of these disclosures are subject to special record-keeping requirements under section 6103(p)(3) and safeguarding requirements under section 6103(p)(4). Disclosures pursuant to section 6103(c), by contrast, are subject to none of those limitations. Moreover, while statutory disclosures are

typically at least partly automated, section 6103(c) waivers typically involve a paper process and are subject to a review for compliance with certain regulatory requirements by the IRS. Roughly 2 million third-party designee consents are processed by the IRS each year. The disclosures required by this bill would add substantially to that number, would be difficult to administer, and would create delay in granting loans and contracts.

Another important consideration relevant to the disclosure of return information under this provision is that many Federal agencies use contractors to administer their loan programs. Contractors may also be involved in the contract approval process. Disclosures under section 6103 may only be made to officers and employees of the recipient agency unless otherwise expressly provided. The Congress traditionally has restricted access to returns and return information by contractors, even when disclosure otherwise has been authorized, due to concerns about taxpayer privacy. In order to protect taxpayer privacy, the amendment to section 6103(l)(3) should make explicit that disclosures to contractors of the agencies administering the loans or entering into contracts will be permitted for purposes only of this provision, subject to the contractors' agreement to otherwise maintain the confidentiality of the information, and subject to the agency's demonstrated oversight of its contractors' compliance with the safeguard requirements of section 6103(p)(4) to the Secretary's satisfaction.

As currently drafted, this provision appears to limit the information to be disclosed to verification of whether or not the taxpayer has a tax debt in delinquent status. Treasury agrees with the decision to so limit the disclosure particularly if disclosures are to be made to contractors. However, we would also point out that the head of a Federal agency is authorized to waive the provisions of section 3720B. Regulations under this section provide examples of the factors that should be balanced in making a decision as to whether to grant a waiver. These factors include the age, amount, and cause(s) of the delinquency and the likelihood that the person will resolve the delinquent debt. 31 C.F.R. §285.13(g)(3)(i). Treasury believes that in some cases, Federal agencies may wish to provide taxpayers with an opportunity to explain a tax delinquency indicator. This is important because, as noted above, significant procedural and systems changes will be necessary to capture this information, and there are likely to be cases where a delinquent status indicator is erroneous. In order to provide such an explanation, however, additional disclosures will be necessary. In such circumstances it will be appropriate to obtain the taxpayer's consent, using existing IRS forms and procedures to disclose that information.

Treasury recognizes the value of the notice provided by requiring taxpayers to authorize the necessary disclosures. Treasury suggests that such notice should be incorporated into the loan application or contract proposal process without such notice having the legal effect of authorizing the disclosures. Partnerships and corporations would be responsible for notifying their 25 percent partners or shareholders that their return information might be disclosed.

#### **Pilot Recommended**

In light of Treasury's policy and technical concerns with the bill, we suggest that if the bill were enacted, it would be appropriate to initiate this program in pilot form. This would permit an overall evaluation of the effectiveness of this program (including its effect on tax

compliance) and would provide the IRS with an opportunity to develop procedures or systems necessary to implement this program.

This concludes my prepared remarks. We look forward to working with the Congress in addressing these concerns as the legislation develops. I would be pleased to respond to your questions.

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Mr. HORN. Carol Covey is the Deputy Director of Defense Procurement for the Department of Defense. Ms. Covey.

Ms. COVEY. Mr. Chairman and members of the subcommittee, thank you for the opportunity to appear before you today to talk about the views of the Department of Defense on H.R. 4181.

H.R. 4181 would prohibit Federal agencies from awarding contracts to individuals who are delinquent in the payment of a tax debt or any other Federal debt. The Department of Defense is concerned that prohibiting the award of contracts to Federal debtors may be more punitive than is necessary and that it may not accomplish the goal of providing an incentive to delinquent debtors to pay their debts but may instead be counterproductive to the prompt payment of Federal debts.

It may be more effective to expand or improve existing programs for collecting Federal debt from contractors than to prohibit the award of contracts to Federal debtors. These programs ensure the government is able to recoup contractor debts in a timely manner.

These programs include the ones mentioned by Ms. Lee earlier, the Treasury offset program for nontax debt, and the IRS levy program for tax debt.

The Department is also concerned that compliance with this bill's requirements would compel Federal agencies to implement a contract clearance process with the Treasury Department to ensure no contract was awarded to a delinquent debtor. This process would undoubtedly delay contract awards until automated systems were implemented. DOD awards hundreds of thousands of contracts annually that could be delayed as a result, and I would like to note that Mr. Turner mentioned potentially setting a threshold at \$2,500 for contract actions. That is the micro-purchase threshold.

If the threshold were set at that level for the Department of Defense alone, we would estimate that the number of actions covered in a fiscal year would be about 6.3 million actions. So we are talking a large number of individual contract actions.

The Department's other concerns are the definition of delinquent tax debt may not provide adequate due process for contractors, particularly if the debt is disputed. We have looked at the definition included in Treasury regulations for delinquent nontax debt, and that appears to be a very satisfactory alternative. It provides due process for debtors, including situations where the debt is disputed.

We would recommend that a similar definition be considered for inclusion in the bill.

The Department is also concerned that the bill could hurt small businesses. A small business that relies on the Federal Government for much of its income may be put out of business if all Federal contract awards stop. This would seem to reduce the probability that the company would be able to repay any debts it owes to the Government.

The bill also currently provides an exception for contracts designated by the President as necessary to the national security. We recommend that the bill be revised to enable the Department of Defense to establish exceptions to meet national security needs rather than maintaining that authority at the Presidential level.

I would add that over the past 6 years or so Congress has acted to streamline the Federal Government acquisition process. The bill

as currently structured is really inconsistent with congressional reform efforts for the acquisition system.

The Department of Defense would be happy, though, to work with the committee staff and with the other agencies to try to recraft the bill into something that administratively is more workable. Thank you for providing me the opportunity to present the Department's concerns with the bill and I would be happy to answer any of the subcommittee's questions.

Mr. HORN. Thank you very much. Those are helpful comments. [The prepared statement of Ms. Covey follows:]

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And Oversight Committee

STATEMENT OF CAROL F. COVEY  
DEPUTY DIRECTOR OF DEFENSE PROCUREMENT  
DEPARTMENT OF DEFENSE  
BEFORE THE  
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION AND TECHNOLOGY  
ON  
H.R. 4181  
"DEBT PAYMENT INCENTIVE ACT OF 2000"

MAY 9, 2000

For Official Use Only  
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House Government Reform  
And Oversight Committee

**Mr. Chairman and Members of the Committee:**

Thank you for the opportunity to appear before this committee to discuss the views of the Department of Defense (DoD) on H.R. 4181, the "Debt Payment Incentive Act of 2000."

H.R. 4181 would prohibit federal agencies from awarding contracts to individuals who are delinquent in the payment of tax debt or any other federal debt. The bill would define a delinquency for a tax debt as an amount not paid within 90 days of an assessment of a tax, penalty, or interest under the Internal Revenue Code of 1986; excluded are debts being repaid in a timely manner under a deferred payment agreement. The bill does not define what constitutes a delinquency for other types of federal debt.

DoD is concerned that prohibiting the award of contracts to federal debtors may be more punitive than is necessary, and that it may not accomplish the goal of providing an incentive to delinquent debtors to pay their debts but may instead be counterproductive to the prompt payment of federal debts. Currently, when federal contractors owe debts to the government, they may be handled in one of two ways:

- The Treasury Department maintains an offset program to collect non-tax debt. Under this program, contract payments owed to a contractor may be used to offset debts the contractor owes to the government. We believe this program has worked effectively to ensure debts owed by contractors are collected promptly and with minimal disruption to the contract payment process.
- Federal agencies routinely report contractor taxpayer identification numbers to the Internal Revenue Service (IRS) when contracts are awarded. This enables the IRS to issue tax levies to the agencies if a contractor has unpaid tax debt. Under this process, contract payments owed to a contractor are used to offset tax debts.

It may be more effective to expand or improve these programs than to prohibit the award of contracts to federal debtors. These programs actually ensure the government is able to recoup contractor debts in a timely manner.

The Department is also concerned that compliance with this bill's requirements would compel federal agencies to implement a contract clearance process with the Treasury Department to ensure no contract was awarded to a delinquent debtor. This

process would undoubtedly delay contract awards until automated systems were implemented. DoD awards hundreds of thousands of contracts each year that could be delayed.

The Department's other concerns are:

- The definition of delinquent tax debt may not provide adequate due process for contractors, particularly if the debt is disputed. The definition in Treasury regulations for delinquent non-tax debt (31 C.F.R. Part 285.13), however, appears to provide due process for debtors, including situations where the debt is disputed. Recommend a definition similar to that included in the Treasury regulations be included in the bill for delinquent tax debt.
- This bill may hurt small businesses. A small business that relies on the federal government for much of its income may be put out of business if all federal contract awards stop. This would seem to reduce the probability that the company would be able to repay any debts it owes to the government.
- It appears that no debt is too small to trigger a suspension of contract awards. A dollar threshold should

be added so contract awards are not suspended because of small debts.

- The bill currently provides an exception for contracts designated by the President as necessary to the national security. The bill should be revised to enable the Department of Defense to establish exceptions to meet national security needs. Additionally, the bill should be revised to permit the Senior Procurement Executive in each agency to waive the bill's requirements in situations where failure to award a contract would have significant unfavorable impact on the agency.

Thank you for providing me the opportunity to present the Department's concerns with this bill. I would be happy to answer any questions you may have.

Mr. HORN. Our last presenter is Sally Thompson, the Chief Financial Officer for the Department of Agriculture. Glad to see you here again.

Ms. THOMPSON. Thank you, and good morning, Mr. Chairman, as well as Congressman Turner and other members of the subcommittee. On behalf of Secretary Glickman, I would like to thank you for the opportunity this morning to discuss House bill 4181.

As you know, we are a steward of a \$104 billion loan and debt portfolio at USDA, and we consider improving debt collection and ensuring the integrity of our loan programs to be a critical part of the mission of our agency.

Your committee and staff always have recognized the significant contributions that these loan programs play in strengthening rural America. Our portfolio includes assistance for socially disadvantaged persons, farm operations, emergency disaster relief efforts, and rural housing and development projects that all require very specialized services. We are the lender of first opportunity for a broad range of Americans who cannot get assistance from other private lending institutions.

We too support the intent of this act to ensure that individuals and corporations that owe debts to the Federal Government must resolve these outstanding issues before qualifying to receive additional assistance from the Federal Government.

We support the provisions that exempt individuals or service providers from the requirement of this act during national disasters or national security efforts because, as you know, we do provide immediate relief and assistance in both domestic and international events.

However, Mr. Chairman, USDA has serious concerns regarding this legislation's provision that require our loanmaking and contracting officers to verify or, in effect, audit with the Internal Revenue that applicants are not delinquent in Federal debt. In other words, we do require a statement that they are not delinquent; and of course if they are, we stop right there. However, this is not an audit, and we do not verify that with the IRS.

This additional verification process would add significant delays to our loanmaking and contracting process.

Currently, program managers rely on the instant information or they wait 2 or 3 days from the commercial credit bureaus or from the Credit Alert Interactive Voice Response system, the CAIVR system; and also we check with Social Security, who has an automated system. We attribute the portion of our low delinquency debt to these credit checks, but as you know for confidentiality purposes the IRS does not report its delinquencies to the on-line credit resources.

I have put up a chart for you, and I see you really can't read it, but trying to give you some sort of an overall view of the volume of agencies, such as USDA loan processing and contracting. In the rural development mission area, farm and foreign agriculture services are our major credit agencies.

In 1999, rural development delivered over 73,000 loans worth \$9.9 billion to rural housing, businesses, telecommunications, distant learning projects, and also infrastructure. In addition to that,

rural development has over 850 county-based offices that create and take in a lot of these loan applications.

In the same fiscal year, our farm and foreign agriculture services made approximately 33,000 nondisaster-related loans for about \$3.6 billion.

Of this total, which is very unique in some respects, FSA made approximately 17,000 of these loans during the time of March and April to finance the production of seed for farmers. Historical records reflect that those majority of our loans are made during that period of time, and so that would say that we are very concerned about the timing and the turnaround that this would add making sure that there was money available for our farmers to get their seed in the ground at the right time.

Also, we have over 2,400 offices that are also processing those loan applications; and when I am beginning to try to paint the picture is how that information would be coming in from all these different locations from all over the country.

In addition to this, FSA is also responsible for administering the Commodity Credit Corporation, which aids producers through loans and purchases and payments and operations, materials and facilities in the manufacturing and marketing of agricultural products, which then also includes exports.

Again, we have a timing on that, and we have made over 207,000 loans last year for a total of about \$8 billion. You begin to get the picture of the magnitude of trying to get this process through IRS and the delays that it might create for us at USDA and, most importantly, for our clients that we are trying to serve.

Several of the people here this morning have also mentioned about the contracting challenges, and I would agree with all of those. We face the same contracting challenges.

I would certainly support the fact that you are looking at putting a pilot program in. I would certainly support the fact that you are looking at a delayed implementation because we too are concerned with systems, not only our own systems that you heard me talk about but also being able to talk to IRS systems as well.

In addition to this, we also would support very strongly some sort of a cap on this. One of the things, I believe, that maybe wasn't even mentioned today but is the smart card that we use for small purchases.

We have over 20,000 people at USDA that have this card. We made over \$1 million worth of purchases last year. It is growing at a very rapid rate, and for us—how do you know, you know, when our people are out there buying a purchase from any number of commercial establishments, whether they have any tax debt or any of their shareholders or principal officers have a tax debt? We also buy off a GSA schedule a lot, and then in those particular cases we do not do the same verification or at least have a signed statement from the business that we are contracting with on their delinquent debt.

We assume that GSA has taken care of that, and that's a concept that hasn't come up this morning as well.

So in conjunction with that, Mr. Chairman, as you know, we have worked very hard over the last couple of years to get our delinquency down and collect those. We have collected over \$136 mil-

lion in delinquent debt this last year through the programs that were mentioned here today, the offset program and other delinquent collection tools. We have increased our collections by over 45 percent from 1999 over 1998, and that was an increase from 1997, as well; and we have also dropped our delinquency over 15 percent in the last couple of years.

Of course, all of these figures, as you know, don't include the tax debt that we are talking about today; but I do think it shows that the criteria that was put in the original debt collection act is working and that it is moving right along.

So, again, as I said, USDA does support the principle of the bill. We agree with both the suggestions that Congressman Turner made this morning, as well as the suggestions that have been made here by GAO, Treasury, OMB, and the Department of Defense; and I would be more than willing to answer any questions you might have.

Mr. HORN. That is very helpful, as usual. I am glad so many of you are at least with it in principle.

I am reminded of "Yes, Minister," that great British show where the career civil servant, Mr. Humphrey, always says, "But, Minister, we agree to that in principle."

[The prepared statement of Ms. Thompson follows:]

STATEMENT OF  
SALLY THOMPSON  
CHIEF FINANCIAL OFFICER  
U.S. DEPARTMENT OF AGRICULTURE  
BEFORE THE  
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,  
INFORMATION AND TECHNOLOGY  
OF THE  
HOUSE COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT  
THE DEBT PAYMENT INCENTIVE ACT OF 2000

May 9, 2000

10 a.m.

Chairman Horn, Congressman Turner, and Members of the Subcommittee, on behalf of Secretary Glickman, I thank you for the opportunity to discuss H.R. 4181, the Debt Payment Incentive Act of 2000. As the steward of a \$104 billion debt portfolio, USDA considers improving debt collection and ensuring our loan programs' fiscal integrity critical elements of our mission.

Your committee and staff always have recognized the significant contributions that these loan programs play in strengthening rural America. Our portfolio includes assistance for socially disadvantaged persons, farm operations, emergency disaster relief efforts, and rural housing projects that require specialized services. In many cases, we are the lender of "first opportunity" for a broad range of Americans whose financial situation precludes them from qualifying for assistance from private lending institutions.

We support the Act's intent to ensure that individuals or corporations that owe debts to the Federal Government must resolve these outstanding issues before qualifying for additional assistance or agreements. We support the provisions that exempt individuals or service providers from this requirement during natural disasters or national security efforts. This exemption recognizes USDA's unique role in circumstances where we provide immediate relief and assistance in both domestic and international events.

However, Mr. Chairman, USDA has serious concerns regarding this legislation's provision that requires our loan-making and contracting officials to verify with the Internal Revenue Service (IRS) that applicants are not delinquent in Federal taxes. This additional verification process would add significant delays to our loan-making and contracting processes. Because IRS does not yet have an online or other readily accessible list of delinquent taxpayers, requiring IRS' involvement in the credit clearance process could disrupt and delay the way in which we serve our customers and enter into agreements with service providers.

**Potential Administrative Challenges**

Currently, program managers with our credit agencies may access applicants' information online to ensure that these individuals meet the statutory and program guidelines. These program managers rely on instant information or wait two-to-three days for data from commercial credit bureaus, the Credit Alert Interactive Voice Response System (CAIVRS), and the Social Security Administration. We attribute a portion of our low delinquency rate to these credit-check methods. For confidentiality purposes, IRS does not report its delinquencies to these credit check resources.

These online resources are increasingly important because they reduce the administrative burden on our staff. Our major credit mission areas, Rural Development (RD) and Farm and Foreign Agricultural Services (FFAS), have implemented significant cuts in their staff. For example, RD has experienced a 28-percent decrease in staff since 1993. At the same time, however, this agency has had to administer a 51-percent increase in program dollars.

Mr. Chairman, let me assure you that the increases in program dollars in this mission area for farm operations and economic development were critical and necessary to USDA's core mission as the steward of rural America. I use this funding discrepancy between staffing and programs to illustrate the difficulties that these agencies face when juggling the responsibilities of delivering time-sensitive program funds and achieving the necessary milestones included in legislation such as H.R. 4181.

In FY 1999, RD delivered nearly 73,000 loans worth \$9.9 billion for rural housing, business, telecommunications, and distance learning projects. RD has about 850 county-based field offices across the country, a majority of which accept loan applications.

In the same fiscal year, FFAS's Farm Service Agency (FSA) made approximately 33,600 non-disaster related loans for \$3.6 billion. Of this total, FSA made approximately 17,000 for \$1.5 billion of annual operating loans used to finance farmers' production expenses. The most critical time period for farming operations nationwide is from pre-planting through planting seasons. This is also the peak demand period for operating capital in many types of farming operations. Historical records reflect that FSA approves the majority of operating loans in March and April. This legislation could cause delays in the application process. Many farmers would receive assistance late in the planting cycle and their production would be adversely affected. The farm economy continues to experience financial stress from low commodity prices due to excess supplies and weak foreign markets. With the current financial difficulties facing agriculture, producers must receive operating credit early in the spring season. Thus, FSA must process applications for annual operating expenses within a timely manner. The current turnaround time is 17 days. H.R. 4181 would require these program managers in the 2,400 FSA county-based offices or their respective state headquarters to clear all applications with the IRS, a process for which no online system exists.

FSA is also responsible for administering most programs funded through the Commodity Credit Corporation (CCC). The CCC aids producers through loans, purchases, payments, and other operations, and makes available materials and facilities required in the production and

marketing of agricultural commodities. In FY 1999, CCC processed about 207,000 applications for participation in its various loan programs worth nearly \$8 billion.

The CCC Charter Act also authorizes the sale of agricultural commodities to other government agencies and to foreign governments and the donation of food to domestic, foreign, or international relief agencies. CCC also assists in the development of new domestic and foreign markets and marketing facilities for agricultural commodities. Applications by borrowers and or producers in the farming community are always time sensitive. Delays in processing application can result in low or no crop yields for these farmers.

In addition to processing the loan applications, both RD and FSA have implemented payment plans that fit our recipients' current financial situation. In the cases of farm operating and housing loans, in particular, unique economic circumstances require flexible repayment plans. We work with farmers or housing residents to devise household budgets or consolidate loans to avoid defaults. This mutual arrangement benefits both the government and the recipient and complies with the mission-related principles on which these assistance programs are based.

#### **Potential Contracting Challenges**

Similar to the loan-delivery areas, USDA's procurement officials also would encounter administrative burdens under H.R. 4181. We have almost 500 contracting officers who managed 157,316 contract actions in FY 1999 worth \$3.8 Billion. Small businesses represented 41 percent, or \$1.5 billion, of these contracts. The provisions included in H.R. 4181 would require acquisition personnel (warranted contracting officers) to verify whether the supplier was delinquent on federal tax items.

Last fiscal year, USDA had more than one million Government purchase/credit card transactions worth \$393 million. Administrative officers, contract specialists, and contracting officers managed these transactions. The passage of H.R. 4181 will also require verification of these suppliers as well. Please keep in mind that there is no current online resource that these contract personnel may use to access this information in a timely fashion.

This legislation also poses additional hardships when awards are made to small businesses. Small businesses often retain experts as consultants on an as-needed basis to bid and perform on a contract. This process allows the small business the flexibility to acquire expertise but limit the cost of retaining the individuals as employees. This minimizes other overhead cost until the business's growth can sustain the added cost.

Contractors already are subject to Debt Collection Improvement Act of 1996 (DCIA) provisions that allow the Federal Government to collect nontax delinquent debt. Our procurement officials have the same online resources to verify business organizations' status regarding nontax debt.

#### **USDA's Progress on Debt Collection**

Mr. Chairman, the DCIA provisions on how to collect nontax debt offer a contrast between the current process and the proposal to include IRS tax debt. We have used the tools given to us by DCIA to assure taxpayers that individuals or contractors with nontax delinquent debt fulfill their obligations to the Federal Government.

In FY 1999, USDA collected \$136.2 million in delinquent debt through the Department of Treasury's Administrative Offset Program (TAOP) and other debt-collection tools. This figure represents a 45-percent increase over the \$93.9 million collected in FY 1998 and a 90-percent increase over the \$71.5 million collected in FY 1997. At the same time, USDA lowered the amount of delinquent debt in its overall loan portfolio from \$7.5 billion in delinquencies in FY 1997 to \$6.4 billion in FY 1999, a drop of nearly 15 percent.

Mr. Chairman, these figures do not include delinquent tax debt owed to the IRS. But the figures illustrate that we are using successfully new tools to comply with debt-collection requirements. Once a borrower or recipient defaults on a loan or benefit, USDA sends the individual or corporation's name to Treasury's debtor file. All federal payments are cross-referenced with this debtor list to check if the individual or business entity owes the government money. If the check uncovers an unpaid debt, the TAOP collects this delinquent debt through offsets against income tax refunds and other payments.

This centralized process has made collecting nontax debt more efficient. We are not aware of any online resource that instantly would link us with an applicant's or business entity's tax record.

We agree on the principle that individuals or businesses that are delinquent in repaying the Federal Government for assistance or contracts should be held accountable for these debts. Perhaps we could discuss using a pilot program to see if agencies could overcome these administrative challenges. We are open to such discussions and look forward to working with you and Ranking Member Turner on our mutual quest to satisfy the taxpayers' request that we collect money owed to their government.

Thank you for your time and consideration, Mr. Chairman. I would be happy to respond to any questions that you or your colleagues may have.

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Mr. HORN. We will get down to the nitty-gritty in these questions. I want to first call on the gentleman from Virginia, Mr. Davis, for 5 minutes of questioning.

Mr. DAVIS OF VIRGINIA. Thank you, Mr. Chairman.

Ms. Lee, let me ask you, in looking at your testimony, you noted—you state I think toward the end, the bill defines a delinquent tax debt as a debt that has not been paid within 90 days of an assessment of a tax penalty or interest under the Internal Revenue Code of 1986. Then you say it is not clear that this definition would provide adequate due process for contractors on disputed debts. That may be right, but isn't that—when I go back to black-listing and everything else—it seems to me that has been one of our concerns that some of the other regulations that have been proposed by OMB and the administration have not provided adequate due process for contracts.

Is this a consistent view, or is this a selective view?

Ms. LEE. Mr. Davis, again and one of the things I tried to emphasize was the flexibility versus the total debarment. In this case, if you get the answer back that yes you are delinquent, whether if its on a recovery program, days, weeks or amounts, the response is you cannot award a contract. Under contractor responsibility, the contractor is asked and given input as to where they are with respect to a debt. There is a requirement for the contracting officer then to discuss those issues with the contractor so they have a process.

There is still a decision to be made at the end, but contracting officers have a little more input. It is not just that we got a report back that said the answer is yes; therefore, I cannot award you a contract. There is a little difference in flexibility.

Mr. DAVIS OF VIRGINIA. Well, there is. On the one hand, though, when you talk about due process you are leaving it in the hands of a contracting officer to make a decision versus the law to make a decision, and you could argue almost that you could get a different outcome based on different contracting officers under your scenario whereas under this scenario at least it is uniform.

Ms. LEE. Correct. Correct.

Mr. DAVIS OF VIRGINIA. OK. I thought it was interesting. We are concerned about that, and that is something I think we will try to address as we move through.

I want to ask some questions about the Circular A-129. This is the policies for Federal credit programs and nontax receivables. Are you familiar with it? It requires agencies to determine whether loan applicants have delinquent Federal debts, including tax debt. A-129 also requires agencies, as I understand it, to include a question on their loan application forms asking applicants if they have such delinquencies.

According to GAO's testimony, agencies are not complying with this directive. Now, what I would ask you is to what extent do you think agencies are complying with the A-129 in asking loan applicants if they have Federal delinquencies? Do you have a feel for that?

Ms. LEE. I don't have a good feel for that. I certainly would be happy to go back and look at the format. There is a lot going on regarding assistance agreements and trying to make that more ac-

cessible to agencies from a standardized format, particularly in grants. I would be happy to look at that and see how we can address that.

Mr. DAVIS OF VIRGINIA. In addition to that, what steps do agencies generally take to ensure that loan applicants are not delinquent on their tax obligation, or is that just ignored right now as a matter of course?

Ms. LEE. Specific tax—

Mr. DAVIS OF VIRGINIA. I will ask anybody else if they would like to address either one of those, too. They may better have a better familiarity in some of the other departments that are doing this hands on every day.

Ms. THOMPSON. Mr. Congressman, when we take a loan application, as it says in the A-129 Circular, there is a question on there that asks, Are you delinquent on your tax debt? Obviously—

Mr. DAVIS OF VIRGINIA. Does anybody ever check that and say they are delinquent?

Ms. THOMPSON. Occasionally, yes. And quite often those are the same ones that show up on the credit checks that we do, and they are delinquent in other areas of debt as well.

My point, in my testimony, was that we don't verify or audit that; and this would require that, and then we got into the processing.

Mr. DAVIS OF VIRGINIA. Don't you argue—that's pretty burdensome to go through and audit all of that, isn't it? Isn't it?

Ms. THOMPSON. Yes, that's what I was saying and certainly until we get the systems in place and we can electronically transfer that information, I tried to give you a feel of the thousands of locations that are making loans.

Mr. DAVIS OF VIRGINIA. Well, let me ask this—and I will ask this to everybody—are agencies contacting the IRS to ascertain the creditworthiness of Federal loan applicants?

Ms. THOMPSON. No, they are not.

Mr. DAVIS OF VIRGINIA. OK. Nobody is doing that right now?

Ms. THOMPSON. Nobody is verifying the information. We ask for tax returns as well, and we get copies of their tax returns. But do we verify those were the actual ones filed with the IRS? No.

Mr. DAVIS OF VIRGINIA. OK. Does everybody agree with that, it is not done as a general rule?

To what extent does the Department of Agriculture screen loan applicants to determine whether they are delinquent on other nontax debts?

Ms. THOMPSON. Every application is verified either through the credit bureau or that CAIVR system.

Mr. DAVIS OF VIRGINIA. How often do you find the loan applicants are delinquent on other Federal nontax debts?

Ms. THOMPSON. I couldn't answer that percentage as well. I would suppose probably about 20 percent maybe.

Mr. DAVIS OF VIRGINIA. OK. I think my time is up. Thank you.

Ms. THOMPSON. Remember the type of clientele that we are doing. We call this our lender of first opportunity. Others call it the last opportunity.

Mr. DAVIS OF VIRGINIA. I understand. Thanks.

Mr. HORN. I yield 5 minutes of questioning to the author of the bill, Mr. Turner of Texas, and then we will go back to Mr. Ose and Mr. Davis.

Mr. TURNER. Thank you, Mr. Chairman.

I think Mr. Davis has perhaps uncovered something we all needed to hear about because apparently we are not doing a very good job of implementing the current A-129 OMB Circular.

It would seem to me that it is important here to be sensitive to the concerns of the Treasury and the IRS in terms of implementation, and I want to work with you to accomplish that.

But I don't—somebody testified just a minute ago that the IRS was performing about 2 million of these type of checks a year. I forget which witness said that. Mr. Mikrut, what was that reference to?

Mr. MIKRUT. Sir, that is with respect to consents, where the taxpayer consents for the release of his tax information to someone else; and that often happens, for instance, if you are looking for a home mortgage, you may give a consent to the bank that they can ask the IRS for certain tax information.

Mr. TURNER. So when they talk about increasing the burden on the IRS, they are already doing 2 million of these type of searches a year now?

Mr. MIKRUT. That is correct.

Mr. TURNER. So it is our obligation, I guess, to try to figure out what the additional burden is going to be here? It is not that the IRS is not doing this. I guess a lot of it is being done manually, done by hand, without the use of some realtime computer system that would give you the answer immediately?

Mr. MIKRUT. That is correct. The consent request is generally a manual paper-type of process; and to the extent you would expand that, for instance, under the student loan application, there may be another 10 million of these such requests. As you know, some sort of system that would be more automated would probably be much more efficient.

Mr. TURNER. All right. I think I tend to agree with you with regard to trying to fine tune our definition or use of the word "assessment." You know, in the bill as originally drafted, we talked about 90 days after the assessment of a tax or penalty; and we also said we were not including debts that were the subject of an installment agreement or a compromise in settlement. Obviously, from what you are saying, we haven't quite gone far enough to ensure that we are not cutting off some taxpayer's right to exercise another step in the appeal process, and we want to clear that up because I don't think any of us have any intent of cutting off anyone's right to appeal to the last step when they have no other recourse and they owe the tax. Ninety days after that is when we want to bar them from Federal contracts or loans.

So help us on that, to get over that hurdle.

With regard to the Department of Defense's concerns, Ms. Covey, I wanted to ask you, you mentioned if we exempt the \$2,500 and below, which I think is an appropriate suggestion, it has been said by several witnesses because you can go in with a government credit card and purchase something under \$2,500 and obviously we

can't check whether those particular vendors owe taxes or not, but you mentioned there were 6.7 million actions, you said.

Ms. COVEY. 6.3 contract awards, 6.3 million contract awards over \$2,500.

Mr. TURNER. How many contractors are there as opposed to contract awards? What we are checking here are contractors, not contracts, however many you have every year. How many contractors?

Ms. COVEY. But we have to do it on a contract-award by contract-award basis, I mean unless you are suggesting, for instance, that if we annually checked for a particular contractor that might be sufficient as well.

Right now we estimate that we are doing business with about, 180,000 contractors annually. We have a central system by which we register them, and that estimate is based on how many are registered in the system.

Mr. TURNER. Well, work with us on this, because obviously we would like to check out the contractors, not every contract. If there are 6.3 million of them. Perhaps we can do a semiannual check and be sure these contractors are paying their taxes or something like that; would be more plausible, I think. As you know, we put a provision in the bill allowing this bar in this legislation to be waived in the interest of national security. We said the President should do it. You suggested it ought to be in the Department of Defense. We don't object to that.

Frankly, I kind of felt like when we put in an exception for national defense we put a hole in the bill you can drive a truck through anyway by the Pentagon, so work with us. We are trying to not get in your way. We are just trying to be sure we accomplish the goal that we all concur on.

Ms. COVEY. We appreciate that.

Mr. TURNER. I think that most of the issues that were raised today were very legitimate ones, and I think that we can, as the staff continues to work with you, resolve every one of them. I don't see any of them that are insurmountable.

The one I am going to struggle with the most is information that reveals that the IRS doesn't have the technical capability to provide this information timely, and I really need to look into that further.

I do think a pilot program of some type with an effective date at a later time for full implementation is probably the right way to go.

Thank you, Mr. Chairman.

Mr. HORN. Well, we thank you and there will be further rounds here. Five minutes for Mr. Ose, the gentleman from California.

Mr. OSE. Thank you, Mr. Chairman.

Ms. Ashby, I want to make sure I understand something that I think you said, and that is that OMB agrees with a connection between awarding additional contracts to nontax delinquent debtors? I wasn't quite sure if I understood you correctly.

Ms. ASHBY. No, I did not say that. I was talking about OMB Circular A-129 that requires agencies—or directs agencies—to check on the delinquency status of prospective loan applicants.

Mr. OSE. OK. Does GAO have a position regarding the concept of barring delinquent taxpayers from receiving Federal contracts?

Ms. ASHBY. Well, as I said in my short statement and as we said in our longer statement for the record, we agree in concept to the barring of delinquent taxpayers.

Mr. OSE. OK.

Ms. ASHBY. But we also recognize that there are key significant implementation issues that need to be resolved, and many of those have been talked about here this morning.

Mr. OSE. Your testimony here this morning also talks about unpaid payroll taxes, which I find one of the most egregious examples of nonpayment. It just kind of drives me nuts. Your testimony highlights an estimate of \$49 billion in unpaid payroll taxes as of September 30, 1998 owed by over 1.8 million businesses?

Ms. ASHBY. That's correct.

Mr. OSE. And this is not a unique occurrence for about 50 percent of those businesses.

Ms. ASHBY. That's right. For about 50 percent, they owed for more than one tax period, more than one quarter.

Mr. OSE. I just wanted to make sure I understood the scope of the issue here.

Ms. Lee, I want to go to a question about one of the things you mentioned. You said that in 1998 there were about \$60 billion worth of nontax outstanding obligations, and that by 1999 that had been reduced to \$53 billion. For that I want to applaud you. I do want to explore that number a little bit.

Did we actually collect \$7 billion in that period of time?

Ms. LEE. Well, I can get you the exact figures, but we have reduced the debt. That could be collection as well as dismissals or for some reason resolution that we weren't going to collect. So I would have to get you the exact number and say whether it was collected.

[The information referred to follows:]

The decrease in total non-tax receivables from \$60 billion in 1998 to \$53 billion in 1999 resulted primarily from a reclassification of \$17 billion of debts in Education's portfolio to a new reporting category called "currently not collectible" (CNC). The new receivables write-off policy incorporated in A-129 permits the use of CNC to accurately portray the true economic value of receivables on the balance sheet, while preserving management options to utilize debt collection tools that will maximize collection of delinquent debt over the long run. For example, student loans, which have no statute of limitations, have a high probability of repayment when debts get older, because former students get jobs and need to establish good credit.

Under the new policy, write-off is mandatory for delinquent debt two years or older, unless agencies can document and justify retaining such debt on their records to OMB in consultation with Treasury. Once debt is written-off, the agency must either classify the debt in CNC or close out the debt on their records as having no value. When debts are closed out, no further debt collection action is to be taken. Whereas cost effective debt collection should continue for CNC debts. Debts written off and closed out increased from \$4.5 billion in 1998 to \$7 billion in 1999.

Actual Government-wide recoveries through debt collection also increased as follows:

	Total non-tax Receivables Outstanding	Total Govt. Collections	Percent Collected
<b>1999</b>	\$ 271 billion	\$ 94.2 billion	35%
<b>1998</b>	\$ 267 billion	\$ 87.6 billion	33%

Source: U.S. Treasury, Financial Management Service

Mr. OSE. So it is not necessarily that we have \$7 billion that we didn't have any more; it is that we have either negotiated, been paid or settled?

Ms. LEE. Correct.

Mr. OSE. \$7 billion?

Ms. LEE. Correct.

Mr. OSE. We might have only had \$1 billion? We might have taken 10 cents on the dollar? We might have gotten a dollar, but we might have only taken 10 cents, too?

Ms. LEE. Correct.

Mr. OSE. OK.

Ms. LEE. Some sort of resolution for that \$7 billion.

Mr. OSE. OK. I just wanted to get it clear in my head that, while the face value of the outstanding amount has reduced, it doesn't mean we have actually put in our pocket a whole bunch more money.

Ms. LEE. Right.

Mr. OSE. OK. I appreciate that.

Ms. Covey, you testified there were 6.3 million contract awards at the DOD that would be subjected to the \$2,500 threshold. How many would be subjected to the \$100,000 threshold?

Ms. COVEY. Less than 100,000 actions.

Mr. OSE. So we basically have like a 97 percent reduction?

Ms. COVEY. Right.

Mr. OSE. So that would go to 100K.

Then in the ag department, Ms. Thompson, how many contracts, if you will, would be affected? Like the DOD has 6.3 million different awards that would be affected if the threshold was set at \$2,500. At the ag department, how many are we talking about?

Ms. THOMPSON. I would say probably about 157,000, and about 500 contractors throughout the country.

That threshold would certainly, as we said, do away with credit card transactions.

Mr. OSE. If we went to the \$100,000 threshold, how many would we have?

Ms. THOMPSON. I would have to get you that number.

Mr. OSE. If you could, please.

Ms. THOMPSON. We do an awful lot of small business. As OMB talked about, probably 41 percent of the contracting business we do are with small businesses so, you know, off the top of my head I would say that it would eliminate a large percentage of those, maybe as much as 50 percent; but I would have to go back and look.

Mr. HORN. Without objection, that letter to the committee and Mr. Ose will be put in the record at this point.

Mr. OSE. Thank you, Mr. Chairman. My time is up.

Mr. KUTZ. Congressman, can I make one point with that? I think it is important to note that most of the 1.8 million businesses that owe those taxes are indeed small, closely held businesses, restaurants, construction companies, etc. So in looking at this threshold, it is important to consider that probably most of the delinquent taxpayers are indeed getting very small contracts in all likelihood. I just wanted to make it understood that the 1.8 million taxpayers are indeed very small businesses.

Mr. OSE. If I could have just a moment, Mr. Chairman.

Mr. HORN. Sure.

Mr. OSE. You bring up an interesting point in that if we have small businesses who are not paying their employee taxes and we set the threshold at \$100,000, then how do we keep from rewarding those people who aren't paying their employee taxes? Are you suggesting we need a stable—

Mr. KUTZ. I am suggesting that the problem is with small businesses so that you need to be cautious in setting a threshold too high so that you are going to—I mean, the big businesses in this country are generally compliant taxpayers. The defense contractors, such as General Dynamics and General Electric and the other ones that are going to do much bigger contracts, they are not the ones that are the problem here. It is generally small businesses we are talking about.

Mr. OSE. I am trying to figure out how to scale the enforcement mechanism, if you will. So I appreciate you bringing that up. That's a good point.

Mr. HORN. The gentleman from Texas, Mr. Turner, for 5 minutes.

Mr. TURNER. Thank you, Mr. Chairman.

Mr. Mikrut, I want to talk to you about a couple of your other suggestions. I think we have resolved that we can come up with language that clears up what we mean by assessment, or do that. I don't see any great problem there.

Your suggestion about limiting the examination of shareholders to those who own 25 percent of the shares of stock in a corporation, I think I mentioned I had suggested 10. Do you see any reason, big reason, to choose 10 or 25?

Mr. MIKRUT. No, Mr. Turner. It is just a matter of how much more of a burden you would have on the administrating agencies and the IRS, but I think there should be some threshold for partnerships as you do have for corporations. I think that would be appropriate.

Mr. TURNER. OK. With regard to the way we carried out the disclosure, our intent here was to be sure that the taxpayers who get loans from the Government and contract with the Government knew that when they contracted or when they apply for a loan, that somebody is going to check and be sure they are current in their Federal taxes. I think I understand why you have suggested we go under 6103(l)(3), and I don't think there is any reason to object to going that route.

If we do what you suggested in your written testimony when you said in order to protect taxpayer privacy the amendment to section 6103(l)(3) should make explicit that disclosures to contractors of the agencies administering the loans or entering into contracts will be permitted for purposes only of this provision subject to the contractor's agreement to otherwise maintain the confidentiality of the information and subject to the agency's demonstrated oversight of its contractor's compliance with the safeguard requirements of 6103(p)(4) and to the Secretary's satisfaction, and we need some help in drafting that language.

If we already are required under the OMB circular to find out if somebody is current in their taxes, I assume that there is some

kind of disclosure process currently ongoing saying that before you get this loan you have to be current in your taxes.

So it seems to me that if we extend that to parties that contract with the Government, that we have probably done all we should have to do to assure that the taxpayer who is the contracting party or who is the loan applicant knows that there is going to be a check to be sure that they are in compliance with this statute.

Does that seem satisfactory to you?

Mr. MIKRUT. I believe so, Mr. Turner. As I understand it, your concern is that the loan applicant or the contracting party should be aware that questions are going to be asked of the IRS regarding their tax status. And you can do that under 6103(1)(3) simply by putting that provision in the contract or in the loan application or some place there, so that the taxpayer knows that's going to happen.

It does not have to be done under 6103(c) under the consent form, although they clearly have notice under consents. It is really a technical tax distinction which subsection you come under, but we think we can accomplish your goals regarding taxpayer notice as well as our goals regarding taxpayer privacy by simply putting it under (1)(3).

Mr. TURNER. Well, work with us on that. I think your suggestions are well taken.

It is an interesting discussion we have had this morning because I almost feel like that it is like a fellow who is walking along and he stumbles into a hornet's nest and the hornets are going everywhere because the truth of the matter is that we have had the requirement in law, not in law but in OMB regulations since January 1993, requiring agencies before they make a loan to find out if somebody owes Federal taxes. And it doesn't sound like to me, from the answers to Mr. Davis' question, that we are doing a very good job of carrying out that OMB circular that's been out there since 1993.

So perhaps that having stumbled into that hornet's nest, it is good we have the opportunity to at least understand that we have a ways to go. And by reaching out and covering tax debt in a more formal way than the OMB circular on loan applicants and extending it to government contractors perhaps might get us in a position where what common sense would tell us becomes reality, and that is if you owe taxes to the Federal Government you shouldn't get the benefits of Federal contracts, nor should you get the benefits of Federal loans.

I think we can resolve the Department of Defense problem, and I look forward to working with you, Ms. Covey, to do that.

Mr. Chairman, thank you for the opportunity to have the hearing this morning.

Mr. HORN. Well, we thank you.

The gentleman from California, Mr. Ose, do you have further questions?

Mr. OSE. Thank you, Mr. Chairman. I did want to cover a comment. I want to commend our friend from Texas for his good work on this. I think he has come across something that I think will be a useful tool in ensuring that. For instance, we get the employee taxes that are supposed to have been collected and to which em-

ployees have basically contributed half from their pay as it relates to Social Security, if nothing else.

So I want to compliment Mr. Turner on that.

I also want to associate myself with the—I don't want to say the amusement, but the irony or the conundrum we face as it relates to the blacklisting issue that Ms. Lee and Mr. Davis and I have discussed on separate occasions as reflected in her testimony today. It did not escape us in my office either, the contradiction, if you will, that seems to be there—it probably isn't, but appears to be there—in the testimony as it relates to the blacklisting issue.

So with that, Mr. Chairman, I will yield back.

Mr. HORN. Well, thank you. I have a few closing questions here directed at Ms. Ashby and Ms. Lee.

In March 1992, during the House Ways and Means Committee hearing, the General Accounting Office said this that in considering the issue of whether tax compliance should be a prerequisite to awarding a Federal contract, "The goal of ensuring that Federal contractors comply with tax laws must be balanced against other national goals."

Now, Ms. Ashby, I am curious. In your testimony today, you state that the GAO supports the concept of barring delinquent taxpayers from receiving Federal contracts, and I am curious what caused the General Accounting Office to change its views on this issue since 1992.

Ms. ASHBY. I don't think we really have changed our views and let me explain. In 1992—and I am very familiar with that testimony because I was an assistant director working for Jennie Stathis who testified, and I probably wrote parts of that testimony, the part dealing with the Federal contractors. And the testimony was delivered in the context of work that we had done where we had actually looked at—compared Federal contract amounts, award amounts, with IRS' records of unpaid taxes, not just payroll taxes. We had numerous examples of contractors who were, in fact, delinquent, who seemed to have resources that could have been used to pay off some of the debt; and our primary focus on that work was to determine how much money IRS might collect by levying the contract payments.

In the course of doing that work and discussing our results, it became obvious that, well, there are numerous cases where there are actually delinquent taxpayers benefiting from Federal contracts and should that be, was sort of the issue we raised. But at the same time, we saw that there were other policy issues. Implementation issues, policy issues—I think the words probably mean a lot of the same things—and we recognized at that time and today that there are numerous public policy goals, one of which is to collect delinquent taxes. And there are others including acquiring goods and services in a cost effective and efficient manner, securing the national defense and so forth.

So it was then and now a recognition that there are multiple issues here that need to be resolved, and we at GAO can't make a recommendation, just as at this point I don't think anyone feels that they can make a recommendation for the answer to this problem. But it is an evolutionary process that we are going through,

and we are getting various viewpoints; and we will get to a workable solution, I am sure.

I think back in 1992 and perhaps even before that, we were pretty much where we are today, that we recognize that there is an issue here. There is an issue of fairness; there is an issue of providing public benefits to those who are not fulfilling their public responsibilities.

Mr. HORN. Well, I think that's well said.

Ms. Lee, do you agree with the GAO's position on this issue?

Ms. LEE. Yes. There is the balance and how do you take into account all of this information and make sure you apply it to relevancy, and how do we make sure that those receiving the Federal benefits, in some case if we really need their product or service or whatever, that we then employ the offset so that we can also recover? It is an interesting balance on how do we make sure that we have those policy issues all moving forward together.

Mr. HORN. Well, I would ask the whole panel here, what is your guess, in your agency, do the benefits associated with this bill outweigh the added costs of the procurement process that were identified by some of the witnesses and some of the statements from various potential witnesses that will be put in the record later?

I am just curious. Agriculture, Department of Defense, Treasury, how would you answer that question, the cost-benefit ratio?

Ms. COVEY. You are saying the cost-benefit ratio—

Mr. HORN. Right.

Ms. COVEY [continuing]. For the Department of Defense as the bill is structured right now?

Mr. HORN. Right.

Ms. COVEY. I think it fails the test. I think the costs associated with the revised process versus the limited benefits to be gained from the bill, I just don't think it meets the cost benefit test. That's why the Department had proposed that we use the systems we already have, the offset system that Treasury administers for nontax Federal debt and the IRS levy program for tax debt and that we look at expanding those systems because we feel that they impact the process, the procurement process, much less than would this type of clearance process.

Ms. THOMPSON. I believe that the cost benefit would certainly be reduced significantly in terms of administrative burden once the IRS had an electronic process where we could send the names in electronically and they could then, within a 2 or 3-day turnaround time, get back to us.

As I mentioned, I am really concerned about farm loans and the amount of the workload during the months of March and April. I think more the cost of it is—the administrative cost is significant, but I think the cost of not getting the money into the farmers' hands, how do you evaluate that? How do you put a dollar amount on to that? That becomes significant.

I think when we talked about loans, mortgage loans, if you think of the amount of time it takes to get a mortgage loan to the private sector, and then you add to that the type of clientele that we are serving out in rural America, you begin to see the amount of the costs there as well.

I am also concerned, of course, as we have talked, Mr. Chairman, about the administrative staff and how that has shrunk so significantly over the last few years, and then you add the burden to that of more administrative work on them, which would then impact the delivery of programs.

Mr. HORN. Well, do you have any studies where you can give us a cost-benefit ratio with some evidence?

Ms. THOMPSON. No.

Mr. HORN. I would ask that of the Department of Defense also. This is off the top of the head, I think, isn't it?

Ms. COVEY. Yes, this is off the top of my head. No, we have no studies to support this.

Mr. HORN. OK. And to what extent are your records electronically available so you could send them over to IRS for that 1 day, 2 day quick that Ms. Thompson is talking about?

Ms. COVEY. It may be in Department of Defense we are a little bit unique because we have a contractor registration system that's on-line. We can give the IRS access to that system. It contains taxpayer identification numbers for every contractor we do business with, other than those where we use the purchase card. So we may be unique in that regard, but we could certainly make that information available to the IRS.

I think an alternative that maybe wasn't discussed this morning was whether the IRS could put up some sort of on-line system where the agencies could automatically access this information on-line.

Again, I think that would resolve a lot of the implementation problems associated with this sort of process.

Mr. HORN. Any comments from the Treasury?

Mr. MIKRUT. I think with respect to the on-line program Ms. Covey mentioned, it would be interesting. I think it would be a great deal of work to get that in a place where it could be effective.

Finally, I think in general, with respect to taxpayer disclosures, we try to limit as many taxpayer disclosures as possible. I think there would be a real concern if the tax information of all taxpayers was suddenly available to any one agency.

For instance, the IRS in the past had put in place implementations to restrict what is known as "agent browsing," that they just can't simply look through taxpayer records without a sufficient reason to, and we have concerns in that respect if all taxpayer information made was available to all Federal agencies.

Mr. KUTZ. Mr. Chairman, let me say something on this, too. I think Congressman Turner's bill provides a preventive control rather than a detective control, and there are some significant benefits to preventing taxpayer delinquencies from ever getting into IRS' records. You are aware that IRS has records of \$231 billion of unpaid taxes, and there is a significant cost to IRS carrying those records over the course of 10 years.

So to the extent that you can prevent delinquencies, you do save the Government some of the administrative costs, incurred by the IRS, including sending out all the various notices and you know all the administrative debt collection processes you have heard discussed today by the various witnesses. To the extent you don't let taxpayers become delinquent, you eliminate those costs up front.

So the bill has a significant benefit not only from the preventive side but for future compliance, which you can't quantify.

Mr. HORN. I think you are absolutely correct on that. What got me started in this business in 1995 was in the Farmer's Home Administration where this multimillionaire had a ranch. He hadn't paid back the mortgage, and he then moved to Santa Barbara, a rather posh place; and he gets another loan to the millions and doesn't pay that back.

How do you let this person get away with it and just sit there?

So I would hope that if you have some real data here as to the impact, fine; but I don't see it when millions are going down the drain and nobody is doing anything about it. At least that's the way it sounds in part of the testimony this morning, that well, you know, we have a problem and so forth and so on.

I think Mr. Kutz is saying if the word gets out, don't mess around with the Federal Government if you have a contract. We know a lot of the major defense contractors have—very little taxes are paid. They have numerous ways to get out of it. We ought to be taking a look at that; and the taxpayers that do pay their bills and pay their taxes would sure appreciate it, in other words, the average citizen.

Would the gentleman from Texas have any further questions he would like to ask this panel?

Mr. TURNER. Mr. Chairman, I just thank you again for the opportunity to have the hearing, and I thank all the witnesses and will continue to work with them to try to come up with a piece of legislation that accomplishes our goals in the least obtrusive and burdensome manner.

Thank you, Mr. Chairman.

Mr. HORN. Well, we thank you.

Let me put a few documents in the record of witnesses that could not be with us today. One is from the National Defense Industrial Association. One is from the Aerospace Industries Association. One is from the U.S. Small Business Administration from the chief counsel for advocacy. And without objection they will be put in the record at this point.

I would like to thank the staffs, both majority and minority, for their work. I think it is a very good panel we have here, and we thank you for coming. J. Russell George, staff director, chief counsel of the House Subcommittee on Government Management Information Technology; to my left, to your right, is Mr. Kaplan. Randy Kaplan is counsel to the subcommittee. Bonnie Heald is director of communications. Bryan Sisk is our clerk. And we have for Mr. Turner, as ranking member; Trey Henderson, his counsel; and Jean Gosa, minority clerk. The court reporter is Mindi Colchico. We have two interns working their hearts out, and that's Elizabeth Seong and Michael Soon.

So with that, we are recessing this hearing until 2 this afternoon. [Whereupon, at 11:30 a.m., the subcommittee was adjourned.]

[Additional information submitted for the hearing record follows:]



*The Voice of the Industrial Base*

**Statement of the National Defense Industrial Association**

**Before the House Government Reform Subcommittee on Government Management,  
Information and Technology Hearing on H.R. 4181, the Debt Payment Incentive Act  
of 2000**

**May 9, 2000**

Mr. Chairman and Members of the Subcommittee

I am Larry Skibbie, President of the National Defense Industrial Association. On behalf of the 25,000 individual members of NDIA and the nearly 900 corporate members who employ the preponderance of the two million men and women who work in the defense sector, I appreciate the opportunity to submit this statement on HR 4181, the Debt Payment Incentive Act of 2000.

Our membership covers the full spectrum of the technology and industrial base, representing every sector of our national infrastructure. Our corporate members range in size from the mega-companies to the small business firms. In fact, nearly forty percent of our member companies are small business.

With regard to HR 4181, this statement summarizes the views received from NDIA members concerning the legislation.

The fundamental aspect of the bill is the disenfranchisement of debtors – that is, preclude receipt of government contracts if money is owed for back taxes. While this may serve as an incentive to pay monies owed, it is predicated on the assumption that the problem is not an inability to pay, but rather an unwillingness to pay.

If the problem is an inability to pay, depriving a company or a person of the opportunity to earn money to pay debts seems self-limiting. If the problem is an unwillingness to pay, then the question is whether withholding award of a contract will serve as a suitable inducement since there has to be a more fundamental problem influencing the behavior of the debtor. Mandatory offset seems a more appropriate solution.

The concerns with this legislation are the following:

- What if the alleged indebtedness is still in dispute?

- What is the impact on procurement lead-time?
- What is the added administrative workload for both industry and government?
- What is the additional impediment to civil/military integration?
- What is the disincentive to commercial companies entering into the industrial base?
- In terms of numbers, most government procurements are micro-purchases for which there is no issuance of a solicitation. In all likelihood, most of the target audience will not be major contractors but small businesses and vendors at the micro-purchase or below level, so you never really get to the root problem area.
- Ownership in corporations of 25 percent or more is something that is rarely static and can easily be circumvented or changed almost on a real-time basis – it has very little to do with the day to day operations of a company in the case of any major corporation. Defining a requirement to identify all corporate officers holding 25 percent ownership and then researching these names appears to create a great deal of paperwork for corporations of any size. It seems the bill is an obtuse and difficult way to approach a problem.
- The bill is focused on the wrong target for the issue at hand. Each corporation has a tax ID, which identifies it in terms of payment of payroll taxes and other corporate matters. It would seem logical to research this for non-payment of payroll taxes.
- Delinquent federal tax indebtedness has little if anything to do with responsibility as a federal contractor. The government has adequate legal remedies to collect these debts and the punitive sanction of contractor debarment should not be added to them. The existing 31 USC 3720B bars persons whose non IRS federal debts are delinquent from federal loans or loan guarantees or federal insurance does not provide a basis for expansion and limitation to IRS indebtedness for these persons and federal contractors. Federal loans, loan guarantees and insurance are dissimilar to federal contracts and should not be treated the same under this statute.

In brief, the Government has the right and should protect itself from doing business with business entities or corporations lacking in business ethics to the extent such issues undermine their integrity or endanger the interests of the Government. However, since this is a matter of “responsibility” which is already addressed in the acquisition regulations and is a prerequisite for contract award, there is no need for legislation as to contracts for goods and services.

Mr. Chairman, this concludes my statement. Thank you again for the opportunity to provide NDIA’s views on HR 4181. We stand prepared to work with the subcommittee on this issue.

**DEBT COLLECTION AND GOVERNMENT CONTRACTING**

Statement by the  
Aerospace Industries Association  
to the Government Reform and Oversight  
Subcommittee on Government Management, Information, and Technology  
United States House of Representatives  
May 9, 2000

Mr. Chairman:

We are pleased to have this opportunity to submit a statement on the impact of H.R. 4181 on our industry. AIA is the trade association that represents the major manufacturers of commercial and military aircraft, helicopters, missiles, satellites, engines, and related aerospace subsystems. Our industry produced \$155 billion of aerospace products last year, and currently employs over 800,000 Americans in high-tech, well-paying positions. Although the proportion of the output of our industry devoted to meeting the requirements of the Defense Department, NASA and the FAA has declined, the U.S. Government remains our largest single customer. Virtually all of our member companies have significant business with these Federal agencies.

We want to begin our discussion by stating our support for the general principle that businesses should be held accountable to pay their Federal debts. Uncollected debts result in unfair additional burdens to all Americans. We support the current mechanisms for ensuring that Federal debt is collected in a timely manner. We further support efforts to improve the efficiency of those existing mechanisms.

Over the years, there have been a number of proposals to add new mechanisms to existing law to improve Federal debt collections and to incentivize the Federal contractor segment of the business community. One of these proposals is the subject of the hearing this morning. We have been asked to comment on H.R. 4181, "The Debt Collection Incentive Act of 2000". The bill would amend section 3720B of title 31, United States Code. Among the changes, the bill would:

- add new language making delinquent Federal debt grounds for ineligibility for Federal government contracts;
- include delinquent debt under the Internal Revenue Code of 1986 (IRC) as a basis for barring a person from receiving financial assistance administered by an agency or from eligibility to enter into a contract with the agency;
- require agency heads to obtain, from each applicant for a Federal loan or loan guarantee or an entity submitting a contract proposal, a form authorizing the Secretary of the Treasury to disclose to the agency information regarding whether the applicant or offeror<sup>4</sup> has any outstanding debt under the IRC that is in delinquent status;

- exempt from the definition of contract any contracts for disaster relief assistance or contracts designated by the President as necessary for the national security of the United States; and
- clarify that, for the purposes of the section, "person" includes any (1) partnership with a partner who has been assessed a penalty under the IRC of 1986 with respect to debt in delinquent status or (2) corporation with an officer or shareholder who holds 25 percent or more of corporate stock in that corporation and who has been assessed a penalty under similar circumstances.

The approach to Federal debt collection embodied in H.R. 4181 was discussed briefly in a General Accounting Office testimony before the House Ways and Means Subcommittee on Oversight on March 17, 1992. On page 7 of the testimony entitled, "Federal Contractor Tax Delinquencies and Status of the 1992 Tax Return Filing Season," the GAO witness stated:

"We believe the last issue we raised—whether tax compliance should be a prerequisite to awarding a federal contract—also deserves consideration. In considering this issue, the goal of ensuring that federal contractors comply with tax laws must be balanced against other national goals. Before acting to change both procurement and tax laws, the Congress would need to understand the public policy implications."

We strongly recommend this approach to the Members of this Committee. Our experience with numerous attempts to impose apparently common-sense procedures on the acquisition process in the Federal agencies is instructive. There are always costs associated with new requirements such as those embodied in H.R. 4181. Further, adding such requirements is contrary to recent congressional and administration efforts to streamline the acquisition process. The proposed legislation would serve as an additional barrier to encouraging commercial companies to offer timely access to commercial technologies and to help the agencies carry out their missions in a cost-effective manner. It would also serve to undercut existing debt collection programs for Federal contractors. Congress should have a clear understanding of how potential benefits to the public will be realized to an extent sufficient to outweigh the added costs.

Our initial assessment of the legislation indicates that the balance between costs and public benefits is at best unclear. We have a number of specific concerns with the impact of the requirements under H.R. 4181. Some of these could be mitigated through changes to the legislation. Others are more fundamental.

#### **IMPACT ON EFFICIENCY**

The procedure required in H.R. 4181 will increase procurement administrative lead times for all Federal agencies. The precise extent is hard to determine in advance, but the scope of the legislation is so broad that it could be substantial. The requirements in H.R. 4181 apply to all procurements of any dollar amount, including procurements of commercial goods and services and simplified acquisitions. There is no limitation on flowing down

the requirements through all the subcontractors under a prime Federal contract, including subcontracts for commercial items and components. Agency contracting officers would apparently be responsible for enforcing the requirements, which presumes that they have been adequately trained and staffed and that necessary additional funds have been appropriated.

Critical to the success of the proposed legislation is the availability of accurate and timely data. We are not aware of any system maintained at the Department of Treasury or in the other Federal agencies that could track delinquent Federal debt in an accurate and timely fashion. The General Accounting Office testimony to this subcommittee in August 1999 indicated serious financial management systems deficiencies that would have to be addressed in a comprehensive manner to prevent the requirements in H.R. 4181 from impacting Federal agencies' missions. Congress would have to invest substantial resources in efficient information systems to approach a workable program covering all categories of Federal debt.

#### **WAIVERS**

Both H.R. 4181 and section 3720B of title 31 do allow for waivers by the heads of agencies and the President. The criteria for such waivers are unclear, however. The phrase "necessary for national security" in section 2(d) of the bill is particularly ambiguous.

#### **IMPACT ON COMMERCIAL ACQUISITION**

For the last 15 years, Federal agencies, supported by Congress, have attempted to increase dramatically the amounts of goods and services they purchase from commercial sources. Such goods and services often embody most advanced technologies at prices set in the commercial marketplace. This initiative has resulted in savings of billions of dollars to the American taxpayer. It has also given our men and women in the armed forces access to advanced technologies much earlier than would be the case under the old system. By imposing a set of potentially costly, unique requirements on Federal contractors, H.R. 4181 would act as a deterrent to commercial companies offering their products to the Federal government as prime or as subcontractors.

Commercial companies will react unfavorably to the added record keeping and the other burdens imposed under H.R. 4181. The requirements in the bill would cover an entire corporation as well as subcontractors for all Federal contracts of any amount. In addition, there is no recognition of the materiality of a delinquent debt and contractors could be barred from competing for a major contract because of a trivial amount of debt. Bidding on large Federal contracts requires a significant expenditure of funds to prepare proposals that are often very complex. Any delinquent Federal debt for any subcontractor or large shareholder could negate this investment by making a contractor ineligible. To forestall such a situation from occurring, contractors would be forced to impose new internal reporting requirements with shareholders and hundreds of subcontractors as a necessary

cost of doing business with a Federal agency. The costs of these reporting systems would have to be added to the product or service price.

#### **IMPACT ON EXISTING REMEDIES**

There are number of existing mechanisms for ensuring that Federal government agencies only do business with contractors that have been determined responsible in accordance with procedures and criteria specified in Subpart 9.1 of the Federal Acquisition Regulation (FAR). These criteria include financial responsibility, as well as integrity, performance, management and technical background, facilities, and ability to perform on time. Contractors that do not meet these threshold criteria are not considered by the contracting officer to be eligible for a particular contract award. In addition, FAR Subpart 9.4 sets forth rules for suspension and debarment of Federal government contractors. These rules include due process procedures including contractor notice and opportunity to comment. Such procedural safeguards are absent from H.R. 4181

Concerning debt collection procedures, the Federal agencies participate in offset programs and tax levies in conjunction with the Internal Revenue Service. These programs allow Federal agencies to benefit from the goods and services provided by delinquent contractors while the IRS continues to collect outstanding debts. To the extent that Federal contractors currently subject to collections under these programs are made ineligible under H.R. 4181, the agencies, the IRS and the American taxpayer would all be the losers by being denied the benefit of their products and services. .

#### **THE BENEFITS RESULTING FROM H.R. 4181 ARE UNCERTAIN**

We are not aware of any analysis that indicates a significant potential for increased collections that would result from the incentives in H.R. 4181. The only recent analysis of which we are aware is the General Accounting Office report to this subcommittee in August 1999 on unpaid payroll taxes (Unpaid Payroll Taxes: Billions in Delinquent Taxes and Penalty Assessments Are Owed, GAO/AIMD/GGD-99-211). Based on matches among the various record keeping systems within the Federal agencies, the GAO determined that only \$507 million of the total of \$49 billion in unpaid payroll taxes as of September 30, 1998 was debt held by Federal contractors. In general, the GAO determined that most unpaid payroll taxes are not fully recoverable and there is often no recovery potential as many of the businesses are insolvent, defunct, or otherwise unable to pay. The GAO report did not assess what marginal improvements in recovery rates might accrue from requirements like those in H.R. 4181 versus relying on increased enforcement of current collection policies and procedures for Federal contractors. Given the uncertainty, we believe that further comprehensive analysis should be undertaken before Congress acts on H.R. 4181.

#### **A CONSTRUCTIVE APPROACH TO FEDERAL DEBT COLLECTION**

Until the Committee receives such analysis, we believe that this Committee should review the existing authorities and programs for debt collection to ensure that they are

achieving their full potential. It is likely agency systems for record keeping could be improved and that reasonable return-on-investment models could be developed to guide further investments. We appreciate the opportunity to present our views and look forward to working with the Subcommittee on addressing this important problem.



OFFICE OF CHIEF COUNSEL FOR ADVOCACY

U.S. SMALL BUSINESS ADMINISTRATION  
WASHINGTON, D.C. 20416

Testimony Submitted for the Record by

Jere W. Glover - Chief Counsel for Advocacy

Before the

Subcommittee on Management, Information and Technology  
Committee on Government Reform  
United States House of Representatives

May 9, 2000

Chairman Horn, Representative Turner and the Members of the Subcommittee:

*Introduction and Summary:* My name is Jere W. Glover and I was appointed by the President and confirmed by the Senate to serve as Chief Counsel for Advocacy. Our office is located in the Small Business Administration and was created over twenty years ago to gather information about and represent the interests of small businesses in matters before the executive agencies and Congress. The opinions I express are those of the Office of Advocacy and may not necessarily reflect the opinion of the SBA or any other federal agency.

I regret that because of prior commitments, I am unable to attend the hearing personally. This is a very important hearing on issues that touch upon small business access to

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federal contracting and loans and the impact that tax related debts have on small businesses. These issues are important to small business owners.

My Office has been asked to review HR 4181, the Debt Payment Incentive Act of 2000, a proposal to amend the Debt Collection Information Act (DCIA) to include tax indebtedness under its umbrella for the first time. The proposal would allow an agency to prevent the award of a contract to a business that has not paid assessed taxes, interest or penalties. We will limit our remarks to the impact on small businesses and not address the administrative problems for federal agencies trusting that the agencies can best address whether there is a problem in that area.

The proposed procedure will have some impact on small business, but we feel that any concern can be overcome by:

- a) not applying it to simplified acquisitions;
- b) having the agency seeking the consent of the bidder and reviewing the bidder's records provided by the Treasury Department only after it is clear that the small business is the likely contract winner, rather than before; and,
- c) allowing a small business 10 days to address the problem unless the business declines to pursue the contract.

**Discussion:** The fair application of the law is important to small business owners. Small businesses are taxpaying citizens and they believe in fair competition. The vast majority of them do not want other businesses, perhaps less responsible businesses, evading taxes while competing for federal contracts or for any other purpose. Therefore, small businesses would not ordinarily oppose the equal application of tax policies.

However, in practice, this bill will only apply to small businesses. Cash flow is a problem for any business but the lines of credit used to solve cash flow problems are much more available to large businesses. For small businesses the most prevalent way to solve everyday cash flow problems in today's system (aside from family resources) is the credit card. For a variety of reasons, a credit card is not the best solution for solving tax

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problems. In a cash crunch, small businesses are left with very limited options to keep the business up and running. Choosing between paying a tax bill and meeting the payroll are often painful.

This is not to say that cash flow problems are unique to small businesses that are poorly run with a bad track record. Cash flow problems can strike any business for a variety of reasons. Even in the federal contracting environment, a contractor or sub-contractor can not always rely on the Prompt Payment Act to work efficiently enough to provide the necessary capital to meet payrolls or pay tax obligations on time. Many federal contracts have progress payments or performance criteria that delay payment pending certain performance benchmarks. Yet benchmarks or not, the small business owner must still meet the payroll; obtain the tools and materials; make timely tax payments, and monthly loan payments. Without a major line of credit to smooth out the peaks and valleys, one interruption in the chain compounds the problem for small businesses. Suppliers might start demanding cash up front for materials needed to start the job. From there, it is a short step to a shortfall on the tax payments. The amendment as proposed could put a small business that is perfectly capable of performing the contract at a tremendous disadvantage compared to a large business with stronger credit line even if that large business is not as well qualified to actually perform the work.

One other point, it is always important (and federal policy) to reduce the amount of paper a small business must file to the absolute minimum. The proposed bill would require a new form to be filed by every federal contract bidder; millions of pages of paper. This is a significant increase in paperwork that should be reduced as much as possible. I think we can solve the small business end of this problem by only requiring the form as part of the due diligence from the apparent contract winner.

*Suggested Amendments* - We believe our concerns about this bill can be resolved with a simple amendment that makes it clear that the procedure does not apply in the case of a purchase under the simplified acquisition procedures (currently purchases under \$100,000 -we believe that is probably what is intended here anyway). The amendment

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should also allow a small business 10 days to “perfect” its debt report after receiving notice that the contract would go to the business except that an unfavorable report based on a Treasury inquiry has been received. Granting ten days moves the responsibility for proceeding with the award of the contract out of the discretion of the contract officer (and the agency) and into the hands of the business owner who can now correct or perfect the report.

If in fact the problem is unpaid taxes, interest and penalties that have been assessed and remain in arrears, then the business can pay them or work out an agreement with the IRS. The business may even be able to use the pending contract to secure a line of credit. Even more important, however, is the case where the bad report results from a mistake in the record or a difference of opinion over the nature and amount of the debt. Under such circumstances, the changes we recommend give the small business a chance to present its side of the case to the agency. For example, the business can show the Treasury computer may not have the latest or most accurate records. It could produce evidence of payment to the IRS or an approved payment plan agreed to by the IRS. Likewise, in a dispute over the amount owed, the business could present mitigating circumstances to the contracting agency that would warrant a waiver in this case.

We hope that this information is helpful to the Committee’s consideration. I would be happy to answer any questions that the Committee might have.



May 9, 2000

The Honorable Jim Turner  
B-350A Rayburn House Office Building  
Washington, DC 20515

Dear Representative Turner:

On behalf of the 600,000 members of the National Federation of Independent Business (NFIB), I am writing in regards to H.R. 4181, the Debt Payment Incentive Act of 2000, which would prohibit delinquent federal debtors from being eligible to enter into federal contracts.

As I am sure you are aware, NFIB sets its policy based on the direct survey of our members. At this time, we do not have any member survey results that would allow us to take a position on this issue.

Also of interest is the fact that a very small percentage of our members actually contract with the federal government. Thus, issues dealing with federal contracting have historically been a low priority for our membership.

Thank you for your inquiry regarding H.R. 4181. I appreciate your interest in our position. Please let us know if you have additional questions.

Sincerely,

  
Dan Danger  
Sr. Vice President  
Federal Public Policy



**THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA**

333 John Carlyle Street, Suite 200 • Alexandria, Virginia 22314 • (703) 548-3118 • FAX (703) 548-3119

RALPH W. JOHNSON, President      ROBERT J. DESJARDINS, Senior Vice President      LARRY C. GASKINS, Vice President  
 FRANCIS W. MADIGAN, JR., Treasurer  
 STEPHEN E. SANDHERR, Executive Vice President & CEO      DAVID R. LUKENS, Chief Operating Officer

May 9, 2000

The Honorable Jim Turner  
 Ranking Member  
 Management Information and Technology Subcommittee  
 B-373 Rayburn House Office Building  
 Washington, DC 20515

Dear Congressman Turner:

The Associated General Contractors of America (AGC) thanks you for the opportunity to comment on the Debt Payment Incentive Act of 2000, H.R. 4181. AGC agrees with the premise that delinquent taxpayers should not receive federal contracts. However, AGC remains concerned about the practical application of this legislation for the following reasons.

**Inaccurate Information**

The inability of the Internal Revenue Service (IRS) to accurately maintain their records jeopardizes federal contractors subject to the proposed scrutiny of H.R. 4181. Recent General Accounting Office (GAO) testimony states:

“System limitations also impede IRS’ ability to prevent, detect, or correct errors to taxpayers’ accounts. As a result, IRS continues to experience delays in posting activity to taxpayer accounts (GAO Testimony May 3, 2000).”

These mistakes and delays could penalize innocent contractors and lead to bid protests, causing delays to the government in a project time table. What recourse will a contractor have should the Department of Treasury provide inaccurate information to a contracting office?

AGC - AMERICA'S CONSTRUCTION ASSOCIATION

**Solution**

To ensure that innocent contractors are not penalized by this legislation, AGC suggests a clarification in the bill that ensures the contracting officer or the Department of Treasury notifies a contractor prior to award that he has been removed from the competitive range because of an outstanding tax debt. This provision should also allow adequate time for the contractor to rebut inaccurate information, to prevent bid protests, and prevent penalizing innocent contractors.

**Subcontractor Treatment**

The legislation does not address the treatment of subcontractors. If the goal is to ensure tax cheats do not receive federal money, then subcontractors need to be held to the same standard. Will named subcontractors such as 8(a) or HUB Zone contractors be subject to the same scrutiny? If so, how will a prime contractor ascertain a subcontractor's taxpayer status? How will the general contractor compel a subcontractor to disclose this information? What penalty will be imposed on a general contractor who employs a subcontractor who has not paid their taxes?

**Long Term Disputes**

H.R. 4181 requires the Treasury Secretary to respond to a contracting officer's inquiry of a contractor's tax status. The Secretary is to report a contractor as delinquent after all administrative remedies have been exhausted and 90 days has elapsed. Information accuracy will be crucial to ensure that no federal contractor is inadvertently penalized.

It is unclear how the legislation would address contractors in a protracted dispute with the IRS. For example, one AGC contractor was told by the IRS to switch from cash accounting to accrual on the basis that the cost of his materials (including subcontractor materials) as a percentage of gross receipts was 15%. The contractor subsequently calculated, however, that the cost of his direct materials (excluding those of his subs) was only 5% of gross receipts. Nonetheless, the IRS insisted that the contractor pay back taxes and interest. This case has been in dispute for more than one year, but this contractor feels he has no choice but to comply with the heavy handed decision of the IRS. Would this contract be eligible for this contract under the changes made by H.R. 4181?

**Solution**

AGC encourages the Government Management and Information Technology Subcommittee to maintain oversight of this process to prevent misapplication of the proposal, to prevent delays in information gathering, and to calculate how many contractors have been rejected for nonpayment of taxes.

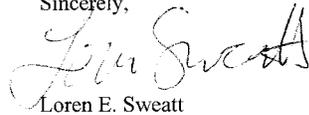
**Contractor Notification**

If a contractor has been suspended or debarred, that individual has received a hearing and been notified of his status. There is no comparable list for prime contractors to consult if a subcontractor is in disfavor with the federal government. In addition, there is a predetermined period of time in which a contractor is ineligible for contracts. How will a contractor know if he is on the IRS list as a delinquent taxpayer? Some federal contracts can take up to one year from submittal of a proposal to award of the project. If taxes are owed and paid during the consideration of that contractor for a project, will the contractor remain ineligible?

**Conclusion**

In light of the bad press the IRS has received over the past few years, is this really a good time to grant them another tool that can be used to coerce innocent businesses into settlements? AGC looks forward to working with the committee to address these concerns.

Sincerely,

A handwritten signature in cursive script, appearing to read "Loren E. Sweatt".

Loren E. Sweatt  
Director, Congressional Relations  
Procurement and Environment



OFFICE OF CHIEF COUNSEL FOR ADVOCACY

U.S. SMALL BUSINESS ADMINISTRATION  
WASHINGTON, D.C. 20416

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