

the use of torture contrary to the outcries of some.

I am glad to cast my vote in support of creating a legal system that will bring to justice those who seek to destroy our way of life. As President Bush said before a joint address before Congress, "whether we bring our enemies to justice, or bring justice to our enemies, justice will be done."

PERSONAL EXPLANATION

HON. MELVIN L. WATT

OF NORTH CAROLINA

IN THE HOUSE OF REPRESENTATIVES

Thursday, September 28, 2006

Mr. WATT. Mr. Speaker, if I was present to vote on rollcall No. 431, I would have voted "no."

INTRODUCTION OF THE WITHHOLDING TAX RELIEF ACT OF 2006

HON. WALLY HERGER

OF CALIFORNIA

IN THE HOUSE OF REPRESENTATIVES

Thursday, September 28, 2006

Mr. HERGER. Mr. Speaker, I have long championed tax relief for small businesses because I believe such firms are the lifeblood of our economy. As a small businessman myself, I know how small business owners struggle to remain profitable in a highly competitive and extremely challenging environment. Yet they continue to be the drivers of much of our Nation's economic and new job growth. It is for this reason that I have strongly supported increases to the current section 179 small business expensing limits, an end to the onerous death tax, and the reduced double taxation of capital gains and dividends. I am concerned, however, that a little known revenue raising provision, passed as part of the tax reconciliation bill in May, will hamper small business' creative spirit by significantly and adversely changing the way governments pay for the goods they use and services they require.

Effective in 2011, section 511 of the Tax Increase Prevention and Reconciliation Act of 2005 will require federal, state, and local governments to withhold 3 percent from payments for goods and services, excluding payments to non-profits and those made by governments with less than \$100 million in annual expenditures. This onerous provision will not take effect for 4 years. But I believe we must begin addressing the impacts it will have on honest taxpaying businesses now, and actively seek alternatives to withholding in the meanwhile.

Every day, thousands of businesses and individuals across the country are reimbursed by governments for various reasons. In my Northern California congressional district, governments rely on local and regional businesses all the time to maintain public services—from the electrician who rewires a city council chambers in Redding to the construction company that builds an interchange at a dangerous stretch of highway in Butte County. When the Feather River needs a new setback

levee, or an existing levee in the network requires urgent repairs to protect the community, the Army Corps of Engineers employs local businesses for construction and materials. Similarly, when an escape route from a fire-prone community requires widening, the government turns to local sources to get the job done. In 2011, however, firms providing these necessary goods and services to governments will see 3 percent of their payments withheld.

I am troubled that the withholding provision will effectively force firms to float a new interest-free loan to the federal Treasury if they do business with a local, state or federal government. In addition, unlike other income-based withholding, which is actually based on tax liability, the new government withholding provision is based on government payments with no relationship to a company's taxable income. This means that, while businesses will be deprived of much needed cash flows for day-to-day operations, the 3 percent provision could end up significantly over withholding for tax purposes. The Joint Committee on Taxation (Joint Committee) confirmed this in its description of the provision, stating "sellers of goods and materials are more likely to have overwithholding and, thus, bear more of the burden of a flat rate because of the lower profit margin on such sales relative to sales of services."

The provision would also disproportionately harm small-and medium-sized businesses that operate on low margins, and contractors that frequently employ subcontractors. It is conceivable that, faced with 3 percent withholding on a revenue source, companies that do business with governments may inflate contract costs to compensate, shift costs to subcontractors, or simply hire fewer employees over the course of the year. Others may resort to increased debt financing to make up for reduced cash flows. In addition, governments at all levels have expressed concerns over the new administrative burdens that such withholding will require.

Among the reasons for inclusion of this provision was a desire to reduce America's tax gap, or the difference between the taxes we believe should be collected in a given year, and those that actually are. The Internal Revenue Service currently estimates the net tax gap to be in the area of \$290 billion. Whether due to taxpayer error or willful tax avoidance, the tax gap is a very real problem that can undermine taxpayer confidence in the voluntary nature of our tax system, and encourage continued non-compliance. According to the National Taxpayer Advocate, the "cost" of the tax gap could be equated to a \$2,000 annual "surtax" on each taxpayer to subsidize non-compliance. The result is that the tax gap ends up "harming compliant taxpayers because they pay their correct tax liability while others do not."

Like many, I believe that bridging the tax gap and encouraging tax compliance should remain a top priority of both Congress and the Administration. Where identification of specific non-compliant sectors of the economy has been difficult, the Administration should continue to investigate ways it can use its existing authority to improve the collection and utilization of non-wage taxpayer information for enforcement purposes. In addition, as better in-

formation on noncompliance is generated, Congress should actively consider whether additional legislation is needed to crack down on tax cheats.

Prior to implementing a new tax collection regime, such as the 3 percent withholding provision, we should investigate what other methods are at our disposal to deal with the outstanding problems of non-compliance. To this end, I believe that any solution that aims to reduce the tax gap should consider the impacts of new burdens on taxpayers. For this reason, I am pleased to introduce the "Withholding Tax Relief Act of 2006," a companion to legislation introduced in the Senate, S. 2831, by Senator LARRY CRAIG of Idaho.

While I recognize the underlying problem of tax compliance must be addressed, I believe this problem—as it pertains to businesses and individuals that provide goods and services to governments—can be tackled in a less intrusive manner than withholding, and with positive results. As reported by the Joint Committee, the withholding provision is estimated to increase revenues coming into the Treasury by \$6.079 billion in its first year of implementation, and between \$215 million and \$235 million per year over the next four years. Further, the Joint Committee recognizes that the "significant revenue effect" in the year of implementation "is largely attributable to accelerating tax receipts," indicating that the additional compliance sought by this provision is really in the ballpark of \$235 million. Still, in order to recapture this amount of unpaid taxes, the withholding provision will affect over \$6 billion of government payments to honest business and individual taxpayers.

It is probably unrealistic to think that we could ever reduce non-compliance to zero, especially given the enormous complexity of our CUITent tax code. But apart from fundamental tax reform and simplification, increased compliance should remain an objective. Congress and the Administration should continue to pursue increased compliance alternatives, including the use of the federal government's already broad authority to levy federal payments, improve coordination and use of taxpayer information, require new information reporting, or increase enforcement. Ultimately, though, any alternatives that focus on compliance should be balanced against the new burdens such compliance mechanisms would cause. We should avoid placing unnecessary burdens on all honest taxpayers in a particular sector of the economy to force the compliance of the few.

Although I recognize that repeal of the 3 percent withholding provision will leave the actual problem of non-compliance unanswered, I believe withholding is the wrong policy approach to this issue. Repeal, as proposed in the "Withholding Tax Relief Act of 2006," serves as a reminder of the importance of this issue, and the need to seriously address the impacts this policy will have on businesses in my congressional district and elsewhere in the country. In addition, we must also begin discussion of alternatives to withholding. I intend to continue working with the business community and others in the 110th Congress on ways to reduce any eventual burdens this provision will cause, as well as alternatives to withholding that will reduce taxpayer non-compliance.