S. HRG. 98-498

TAX REFUND OFFSET PROGRAM FOR DELINQUENT STUDENT LOANS AND CHILD SUPPORT PAYMENTS

HEARING

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT OF THE INTERNAL REVENUE SERVICE

OF THE

COMMITTEE ON FINANCE UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

ON

S. 150

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TAX REFUND OFFSET PROGRAM FOR DELINQUENT STUDENT LOANS AND CHILD SUPPORT PAYMENTS

FRIDAY, SEPTEMBER 16, 1983

U.S. SENATE,
COMMITTEE ON FINANCE,
SUBCOMMITTEE ON OVERSIGHT
OF THE INTERNAL REVENUE SERVICE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:38 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Charles E. Grassley (chairman) presiding.

Present: Senator Grassley.

[The press release announcing the hearing, background material on the child support enforcement program and on S. 150, and Senator Grassley's prepared statement follow:]

[Press Release]

FINANCE SUBCOMMITTEE ON OVERSIGHT OF THE INTERNAL REVENUE SERVICE SETS HEARING ON TAX REFUND OFFSET PROGRAM AND S. 150

Senator Charles E. Grassley (R., Iowa), Chairman of the Subcommittee on Oversight of the Internal Revenue Service of the Committee on Finance, announced today that the Subcommittee will hold a hearing on Friday, September 16, 1983, on the general effectiveness of the tax refund offset program for certain delinquent child support payments and S. 150.

In announcing the hearing, Senator Grassley noted that "the tax refund offset program for delinquent child support payments has been part of the Internal Revenue Code since the passage of the Omnibus Reconciliation Act of 1980. The Subcommittee intends to examine the effectiveness of the program, the possibility of extending the refund offset program to non-AFDC recipients and the applicability of this approach to other delinquent Federal accounts." Senator Grassley stated that the Subcommittee intends to examine the effect of this program on voluntary compliance with the Federal revenue laws and the recent court decisions on the refund offset program.

The hearing will begin at 9:30 a.m. in Room SD-215 of the Dirksen Senate Office Building.

The following legislative proposal on a similar issue will also be considered at the hearing:

S. 150.--Introduced by Senator Jepsen. S. 150 generally would provide for the collection of delinquent student loans, guaranteed by the Federal Government, by offsetting any tax refund due delinquent debtors.

DESCRIPTION OF THE CHILD SUPPORT ENFORCEMENT PROGRAM AND OF S. 150 (THE "COLLECTION OF STUDENT LOANS IN DEFAULT ACT OF 1983")

SCHEDULED FOR A HEARING

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT OF THE INTERNAL REVENUE SERVICE

OF THE

SENATE COMMITTEE ON FINANCE

ON SEPTEMBER 16, 1983

PREPARED BY THE STAFF

OF THE

JOINT COMMITTEE ON TAXATION

INTRODUCTION

The Subcommittee on Oversight of the Internal Revenue Service of the Senate Committee on Finance has scheduled a hearing on September 16, 1983, to examine the effectiveness of the Federal tax refund-offset provisions for collecting certain delinquent child support payments owed to recipients in an Aid to Families with Dependent Children (AFDC) program. The hearing also will examine the possibility of expanding these, or similar provisions, to other types of delinquent Federal accounts. Specifically, the Subcommittee plans to examine the possible effectiveness of such refund-offset provisions for collecting delinquent child support payments in the case of non-AFDC recipients and to examine S. 150 (introduced by Senator Jepsen) which generally would provide for the collection by the Internal Revenue Service of certain delinquent student loan amounts guaranteed by the Federal Government.

The first part of this pamphlet is a summary of the present child support enforcement program and of S. 150. The second part contains a more detailed description of the child support enforcement program and an overview of some recent court decisions involving the refund-offset provisions which are a part of the program. The third part of the pamphlet contains a more detailed description of S. 150, including present law, explanation of provisions, and effective date.

I. SUMMARY

The Child Support Enforcement Program

Present law provides for Federal assistance in collecting delinquent child support payments from absent parents. This program includes both tax and non-tax aspects. The applicable tax provisions include authorization for the Internal Revenue Service to assess and collect, in the same manner as a tax, amounts reported to it by the Secretary of Health and Human Services as delinquent when State agencies have been unable to collect the sums by other means. An additional collection method is provided by which the IRS can offset Federal income tax refunds otherwise due absent parents of children who receive AFDC payments owing delinquent child and spousal support payments against the delinquent payments and remit the tax refunds to the appropriate State welfare agencies.

Because tax information generally cannot be disclosed except in strictly limited circumstances, the disclosure provisions of the Internal Revenue Code include a special exception permitting disclosure of certain tax information by the Internal Revenue Service solely for the purpose of establishing and collecting these delinquent child support payments and locating individuals owing child support.

S. 150

S. 150, introduced by Senator Jepsen, would provide a new Federal program administered through the tax system for collecting student loans in default which the Federal Government has made or guaranteed. Under the bill, the Internal Revenue Service would collect amounts in default on Federally guaranteed student loans and apply those amounts (through the Department of Education) against the unpaid loan balances. The program generally would be structured in a manner similar to the present assessment and collection provisions for delinquent child support obligations as opposed to the refund-offset provisions.

The provisions of the bill would be effective on January 1, 1984.

II. DESCRIPTION OF THE CHILD SUPPORT ENFORCEMENT PROGRAM

A. Present Law

Overview of program

Title IV-D of the Social Security Act, enacted in 1975, established a Federal program for enforcing child support obligations of absentee parents. The program provides services both to families receiving benefits under an Aid to Families with Dependent Children (AFDC) program and to non-AFDC families. The child support enforcement program is designed to locate absentee parents, establish paternity, and assist in the establishment and collection of child support payments, whether court-ordered, administratively determined, or voluntary.

As a condition of eligibility for AFDC payments, each applicant or recipient must assign to the State any rights to support which he or she may have in his or her own behalf or on behalf of children in the family and must cooperate with the State in establishing paternity and in collecting support payments. States are also required to provide child support enforcement services to families that are not eligible for AFDC; however, one of the two Federal tax enforcement provisions (the refund-offset provisions) does not apply in the case of non-AFDC families.[1]

Effective on July 1, 1975, the Internal Revenue Service was authorized to assess and collect, in the same manner as a tax, amounts certified by the Secretary of Health and Human Services (HHS)[2] as delinquent child and spousal support payments (Code sec. 6305(a)). The Internal Revenue Code further provides that no court has jurisdiction to review Federal assessment or collection activities under this provision. This prohibition is similar in nature to the anti-injunction provision that generally bars suits to restrain assessment or collection of Federal taxes (sec. 7421).

The Omnibus Budget Reconciliation Act of 1981[3] amended the child support enforcement program to provide for collection of past-due child and spousal support by offsetting Federal tax refunds as an additional method of insuring payment of the support in the case of families receiving AFDC payments (sec. 6402(c)). That act also expanded the authority of prior law to enforce support obligations for support of the parent with whom the child is living, required States to have programs to collect child support obligations which are being enforced by reducing unemployment benefits of absent parents, and made other non-tax changes in the program.

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[1] S. 1708, introduced by Senator Grassley, would extend the Federal tax refund-offset provisions of the child enforcement program to non-AFDC families.

[2] Formerly the Secretary of Health, Education, and Welfare.

[3] Public Law 97-35.

The 1981 refund-offset provisions do not contain express anti-injunction provisions like those of the direct assessment provision.

Disclosure of tax information

In general, tax returns and return information are confidential and may be disclosed by the IRS only in certain strictly regulated circumstances (sec. 6103). Violation of these disclosure provisions may result in imposition of fines or prison terms as well as civil damage liability. For this purpose, return information generally means all information included on a person's tax return as well as other information obtained by the IRS that is related to the return or to the determination of tax liability. For example, information as to a taxpayer's identification, the nature and source of his or her income, and the amount of any refund due him or her, is return information.

As part of the Federal child support enforcement program, an exception is made to the general disclosure rules permitting certain disclosures to Federal, State, or local child support enforcement agencies of information on the address, filing status, amounts and nature of income, and number of dependents claimed on the return of a person owing delinquent child support payments. Additionally, the payors of the person's income may be disclosed if that information is not reasonably available from any other source. These disclosures are permitted only for the purposes of, and to the extent necessary in, establishing and collecting child support obligations from, and locating individuals owing the support obligations (sec. 6103(l)(6).

Administration of the refund-offset provisions

Beginning with tax returns filed in 1982, income tax refunds were withheld by the Internal Revenue Service in certain cases and used to pay delinquent child and spousal support (sec. 6402(c)). Under these provisions, the names of persons owing more than $150 in child or spousal support payments and who are at least three months in arrears are reported to the IRS by States through the Office of Child Support Enforcement of the Department of Health and Human Services. HHS consolidates the lists from the individual States and sends the IRS a single nationwide computer tape. IRS then compares the tape with its records and offsets refunds in whole or in part against support payments shown due. Offset refunds are reported to HHS monthly and HHS then arranges for payment to State welfare agencies for further disbursement to local agencies, as necessary.

When all or part of a person's refund is withheld, the IRS notifies the person in writing of the offset. If the taxpayer wishes to contest the action, however, appeal is to the State welfare agency rather than the IRS. If a refund is erroneously offset, the State welfare agency, not the IRS, must reimburse the person whose refund was withheld.

In some cases, the offset refund may be from a joint return filed by a person who is delinquent in making support payments and a spouse who is not obligated to pay the support. If such an offset occurs, the spouse not obligated to pay support may file a claim with the IRS for the portion of the withheld refund attributable to

his or her income. To receive the refund, however, the spouse must provide information necessary to allocate the income and deductions on the joint return so that each spouse's tax liability may be calculated. If such information is not provided, the IRS will allocate the refund according to an established formula (Rev. Rul. 80-7, 1980-1 C.B. 296).

The IRS is entitled to bill (through HHS) the States benefitting from the refund-offset provisions in an amount sufficient to reimburse it for costs it incurs in offsetting refunds for payment of delinquent child and spousal support.

B. Recent Court Decisions Involving the Refund-Offset Provisions

Implementation of the refund-offset provisions has resulted in several court challenges to its constitutionality. Three recent United States District Court cases illustrate the nature of these challenges. Because the refund-offset provisions were only enacted in 1981, appellate courts generally have not addressed the issues raised by the provisions; however, appeals are pending in the United States Circuit Courts in two of the cases discussed below, and in another case which was dismissed as moot.[4]

Sorensen v. *Secretary of the Treasury*

On December 28, 1982, the United States District Court for the Western District of Washington addressed the nature and legality of the refund-offset provisions in *Sorensen* v. *Secretary of the Treasury*.[5] In *Sorensen*, the Court first addressed the issue of standing of the taxpayers to enjoin enforcement of the provisions. The Court held that the refund-offset provisions do not involve assessment or collection of a tax since the United States is merely a transfer agent, and therefore, persons deprived of their refunds have standing to sue, notwithstanding the provisions of the tax law generally prohibiting suits to enjoin the assessment or collection of tax.

The Court then addressed the issue of whether the procedure by which a refund is offset violated constitutional due process guarantees. The *Sorensen* case involved a spouse signing a joint return who did not owe an obligation of support and the nature, under State law, of the interest of the delinquent parent in the income of that spouse. The Court held that the IRS notice procedures violated constitutional due process guarantees, stating that the absence of specific notice by the IRS to the non-obligated spouse that the entire refund would be offset unless she filed an additional claim, but that only one-half of the refund was subject to offset under the applicable Washington State community property law, rendered the notice insufficient to apprise the spouse of her rights.

Nelson v. *Regan*

On January 14, 1983, the United States District Court for Connecticut addressed similar due process challenges to the refund-offset provisions in *Nelson* v. *Regan*.[6] The *Nelson* case also involved

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[4] *Rucker* v. *Secretary of the Treasury*, 555 F. Supp. 1051 (D. Colo. 1983), *appeal docketed* (10th Cir.).

[5] 557 F. Supp. 729 (W.D. Wash. 1982), *appeal docketed* (9th Cir.).

[6] 560 F. Supp. 1101 (D. Conn. 1983), *appeal docketed* (2nd Cir.).

a spouse who did not owe an obligation of support, but who signed a joint return which led to her tax refund being offset against her husband's unpaid support obligation. In *Nelson*, the Court held that a clear "predeprivation notification, specifying the possible defenses and the procedures for asserting those defenses" is constitutionally required under the due process clause. The Court further held that the State welfare agency must provide the opportunity for precertification administrative review of its determinations by an official with authority to remove names from any list of delinquent debtors to be certified to the IRS before any offsets can occur.

Vidra* v. *Egger

In *Vidra* v. *Egger*,[7] the United States District Court for the Eastern District of Pennsylvania viewed the refund-offset provisions as part of the tax collection process. In *Vidra*, spouses of fathers owing delinquent child-support payments sued to enjoin enforcement of the refund-offset provisions, alleging that they violated constitutional due process guarantees. Before the suit, the IRS had informed the spouses that their remedy was against the Pennsylvania welfare agency, and the spouses had not, therefore, filed claims for refund of the offset amounts with the IRS. The Court dismissed the case, citing the anti-injunction provisions of the Code and stated that a refund suit was the only Federal remedy available.

[7] 83-1 USTC ¶ 9158 (Dec. 8, 1982).

III. DESCRIPTION OF S. 150

(THE COLLECTION OF STUDENT LOANS IN DEFAULT ACT OF 1983)

A. Present Law

Overview of Federal guaranteed student loan program

Under present law, the Federal Government guarantees or insures all or a portion of certain types of loans made to students by State governments and other persons with whom the United States has agreements under Federal aid to education programs. As a result, if a student borrower under any of these programs defaults on payment of interest or principal, the United States may be be forced to repay the amount in default. In case of default, the United States is authorized to sue in any State or Federal court having general jurisdiction to enforce payment or to compromise any claim arising under any such guarantee or insurance agreement. However, present law includes no program for collecting, through the tax system, student loan amounts in default.

Disclosure of tax information

In general, tax returns and return information are confidential and may be disclosed only in certain strictly regulated circumstances (Code sec. 6103). Return information includes a taxpayer's identification and the nature and source of his or her income. However, present law provides an exception to assist in evaluating applicants for Federally insured loans. Under this exception, the Secretary of the Treasury may disclose to the head of any Federal agency administering any program under which the United States (or any Federal agency) makes, guarantees, or insures loans, whether or not an applicant for a loan under any such program has a tax delinquent account. This disclosure may be made only for the purpose, and to the extent necessary, to determine the creditworthiness of the loan applicant (sec. 6103(l)(3)).

Another exception permits the Secretary of the Treasury, upon written request from the Secretary of Education, to disclose the mailing address of any taxpayer who is in default on any Federally insured student loan made with respect to higher education or made with respect to certain student assistance programs. (See, sec. 6103(m)(4) and the Higher Education Act of 1965, Title IV, parts B and E, 20 U.S.C. sections 1001, *et. seq.*) In addition, the Secretary of Treasury may disclose the mailing address of any taxpayer who has defaulted on certain loans made under the Migration and Refugee Assistance Act of 1962 to a student at an institution of higher learning (sec. 6103(m)(4)).

These disclosures may be made for use by officers, employees, or agents of the Department of Education to assist in locating the defaulting taxpayer and collecting the unpaid amounts. These disclo-

sures may also be made to any lender, or any State or nonprofit guaranteeing agency participating in loans under the Higher Education Act of 1965, for use by such persons in collecting such loans.

B. Explanation of Provisions

Both the Internal Revenue Code and the Higher Education Act of 1965 would be amended by the bill to establish a new Federal program administered through the tax system for collecting student loans in default.

Amendments to the Internal Revenue Code

Under the bill, a new section dealing with the collection of student loans in default would be added to the Internal Revenue Code (new sec. 6306). Under this provision, in the case of calendar year taxpayers, the Secretary of Treasury would be required to give written notice, no later than January 15 of each calendar year, to each individual with respect to whom that Secretary has received notice under the provisions of the Higher Education Act of 1965 of a default in payments. The notice would be required to explain the provisions of the new collection program, the dollar amount which the individual must pay, and instructions for making payment. If an individual had a taxable year other than a calendar year, notice would be required to be sent no later than 15 days after the close of that taxable year. The amount specified as due at that time would be the amount owing as of the last day of that taxable year.

Amounts collected by the Secretary of the Treasury under this provision would have to be paid in connection with the filing of the taxpayer's income tax return for the taxable year preceding the year in which he or she receives the notice. If an individual failed to pay the full amount required to be paid on or before the due date of the income tax return for that taxable year, the Secretary of the Treasury would assess and collect the unpaid amount as if such amount were a tax, the collection of which would be jeopardized by delay.

The bill would include specific anti-injunction provisions applicable to the new program. No court of the United States would have jurisdiction of any suit brought to restrain or review the assessment or collection made by the Secretary of these delinquent amounts. In addition, no such assessment and collection would be subject to review by the Secretary of Treasury in any proceeding. However, the bill would not preclude any action against a State by an individual to determine his or her liability for any amount assessed and collected, or to recover any such amount.

The Secretary of the Treasury would be required to report to the Secretary of Education, at least monthly, the amount collected under this program. Amounts collected under the program would be transferred by the Secretary of Treasury to the Secretary of Education at the end of each calendar quarter for disposition as described below.

Amendments to the Higher Education Act of 1965

The Higher Education Act of 1965 would be amended to require the Secretary of Education to provide the Secretary of the Treasury

with a list showing the name and last known address of any person who has defaulted on a loan made, guaranteed, or insured by the United States. In addition, the notice would have to state the amount of unpaid principal and accrued interest on each such loan and the name of the holder of each loan. This list would be provided at the end of each calendar quarter.

Loans would be subject to collection under this program if they were in default for at least 6 months at the time the transmittal was made, and either (1) the United States was an assignee of the note (or other evidence of indebtedness) or (2) the note was held by a State, a nonprofit institution, or other specified type of holder and guaranteed by the United States and the amount of the unpaid principal and accrued interest had been determined by a court or by State administrative process.

Amounts collected by the Secretary of the Treasury under this program would be transferred to the Secretary of Education for disposition in accordance with the guarantee agreement between the United States and the State or other organization involved in the loan. Amounts due the Federal Government would be deposited in the general fund of the Treasury.

C. Effective Date

The provisions of the bill would be effective on January 1, 1984.

STATEMENT OF SENATOR CHARLES E. GRASSLEY

Today, the Subcommittee on the Oversight of the Internal Revenue Service is holding a hearing to examine the present federal income tax offset program for child support enforcement. Furthermore, we will be looking at the feasibility of including non-AFDC families with delinquent child support in this program, as well as expanding the refund offset program to include other overdue Federal debts such as delinquent student loans.

Child support enforcement is an issue resulting from many unfortunate changes in the structure of American families in the past several years. Over one million American marriages end in divorce each year, resulting in a growing number of children living in single-parent families. At the present time, approximately 87 percent of the families receiving Aid to Families with Dependent Children do so due to a living parent's absence from the home. Over 38 percent of the children in AFDC households were born to unmarried parents. These fathers have an obligation to support their children which has been assumed by the Federal agencies. These changes have increased the costs of welfare payments to many of these single-parent families.

In 1978, 7.1 million women in America were mothers of one or more children under the age of 21 whose fathers were not present in the home. Four out of every ten of these women were dependent for the support of their children on sources other than the fathers of these children. Sixty percent of these 7.1 million women had been awarded child support payments, but many had not received the full amount of support they were due. Of the 3.4 million women due child support payments in 1978, only one-half received the full amount. Approximately 23 percent received no payment at all. Failure for fathers to pay child support is not related to a parent's income or the size of the support payment. High-income absent parents are just as likely to avoid their obligations as low-income absent parents.

As I am sure you are aware, section 451 of the Social Security Act created the child support enforcement program "for the purpose of enforcing the support obligations owed by absent parents to their children, locating absent parents, establishing paternity, and obtaining child support." This program is designed to reduce welfare spending by returning the responsibility of supporting children to the parents. One issue we must investigate today is the effectiveness of the child support enforcement

program in reducing government welfare costs weighed against the additional burden it creates for the Internal Revenue Service. We must also look at recent trends which indicate that collections on behalf of AFDC recipients have turned downward, exclusive of the income tax refund offset program, and examine the reasons for this trend.

The Federal income tax refund offset program was designed to expand child support obligations of absent parents whose children are receiving cash assistance through AFDC. Public Law 97-35 required the Internal Revenue Service to establish a tax offset program for past due support obligations, and required the States to submit appropriate lists of delinquent individuals to the Office of Child Support Enforcement.

Under the offset program, all States are required to submit to the Office of Child Support Enforcement a certified list of individuals who are delinquent on legal child support obligations for families who receive AFDC payments. The States must have made a reasonable effort to collect the amount owed in order to be eligible for the offset. Other requirements must be met in order for the offset program to be implemented. After certified lists are submitted by the State, OCSE, reconciles the lists and forwards the lists to the IRS. Cases which are matched are offset by any refund due and a notice is sent to the delinquent individual. Lists of obligations and collected funds are then referred back to OSCE for return to the State. The State then receives the collections which were made, as well as a listing of home addresses of the absent parents whose refunds were offset. These lists enable the State agencies handling child support enforcement to locate absent parents for further enforcement by the State or local agencies. The Office of Child Support Enforcement bills the State for processing costs for each case in which an offset was made. We need to discover the total federal costs of offsetting tax refunds for AFDC recipients and attempt to analyze the effect of the offset program on taxpayers' willingness to comply with our tax laws.

I think it is important that we look at the cost effectiveness of the tax refund offset program as it affects collections made, as well as what it costs Federal agencies to implement the tax refund offset program. Has this program been cost effective? Would it be cost effective to expand the Federal income tax refund offset program to include non-AFDC families? Since non-AFDC families are not currently on the Federal rolls, can we justify including these families in the refund offset program without a Federal debt obligation? Is new legislation needed to include non-AFDC families in this program? Or should this be an administrative change?

In the past, Congress has been reticent about using the Internal Revenue Code as a debt collection vehicle. However, due to the enormity of the delinquent child support problem, can we justify the use of the Tax Code to collect the overdue payments?

Another issue to be discussed today is whether or not refund offset programs should be implemented for the collection of other overdue Federal debts. Senator Jepsen has introduced a bill, S. 150, which would ask the IRS to collect delinquent government guaranteed student loans. Again, questions similar to those stated above need to be asked. Although this is a very meritorious bill, should the tax code be used as a vehicle to collect unpaid student loans? Are any other means available for this purpose? These are issues we hope to successfully define and find answers to today.

Before we begin our hearing, I would like to thank a departing Joint Committee staff lawyer, Ben Hartley, for all of his help on agricultural and estate tax issues. His assistance on special use valuation estate tax reform, PIK, soil conservation tax credits and other issues has been very helpful to me. He truly understands the concerns of my constituents and his departure will be felt by all of us with agricultural concerns.

Senator GRASSLEY. I would like to call to order the hearing of the IRS Oversight Subcommittee on the issue of the income tax offset as might be used in child support assistance recovery, and also in the area of recapturing money owed to the Federal Government on education assistance.

I'm calling this meeting to order, let my state that I have a statement that I am going to insert in the record as opposed to reading it, with the purpose of saving time. We need to conclude by 1 o'clock so that a follow-on committee hearing by the Finance Committee can be held.

We are following the work of other subcommittees on finance in explaining this topic, it is with the hope that we can move this legislation.

We have found in the area of public supported families that the income tax offset has worked tremendously well, and this legislation would broaden the offset to nonpublic-support families to see if the practice can be broadened to accomplish the good of having those people who have an obligation, legal and otherwise, to support their families so do.

It is my pleasure to have at the witness table a person I have come to know well, Commissioner Roscoe Egger. He has testified many times and is a pleasure to work with on all subcommittee issues.

We also have at the table Ronald Pearlman, Deputy Assistant Secretary of the Treasury, so that he can testify, and we can have the panel answer questions at the same time.

I would ask you to proceed, Commissioner, and then Deputy Assistant Secretary Pearlman. And then we will ask questions of both of you.

Commissioner EGGER. Fine.

STATEMENT OF HON. ROSCOE L. EGGER, JR., COMMISSIONER, INTERNAL REVENUE SERVICE, WASHINGTON, D.C.

Commissioner EGGER. Well, Mr. Chairman, I am delighted to be here today to talk about this program to collect past-due child and spousal support debts by income tax refund offset.

In the full statement that I have prepared I will go into some depth on certain of the legal issues, but for the purpose of the oral testimony I would like to simply outline the program and give you some examples of some of the problems that we have encountered.

I have here with me Stanley Goldberg, who is the Assistant Commissioner for Returns and Information Processing. He is conversant with all of the details, so I think among the three of us we will be able to answer most of the questions that you or any other member of the subcommittee might have.

Senator GRASSLEY. Thank you.

Commissioner EGGER. The Government's efforts to collect past-due child and spousal support from Federal tax refunds were instituted as part of Public Law 97-35, the Omnibus Budget Reconciliation Act of 1981. That act, approved in August 1981 and effective on October 1 of that year, that is, the start of fiscal year 1982, provided in general that individual income tax overpayments—that is, refunds—may be offset to the extent of certain deliquent child and spousal support obligations.

Data on the individuals involved, the existence of these obligations, and the amounts to be offset are validated by the States and then sent to the Office of Child Support Enforcement of the Department of Health and Human Services. HHS then forward this information to the Service. We started offsetting refunds under this program in January 1982.

To better understand our role in the program, let me briefly describe how a sample case might work. For ease of discussion I have

a simplified case, but you should be aware that in many instances these cases can get quite complex.

An obligation for child or spousal support arises typically from a court or administrative order, as a result of divorce or separation. When and if the spouse with the obligation fails to meet it, the other spouse with the custody of any children may be forced to seek assistance under the aid to families with dependent children program, which is funded by HHS and administered by the States.

As a condition of receiving AFDC assistance, the spouse must assign his or her rights to support payments to the welfare agency of the State that is involved. The State has an obligation under Federal law to verify that the information on those payments is correct and to try to collect that support, and then as part of that responsibility they refer uncollected cases to the Internal Revenue Service through HHS. This is done on an annual basis.

The Service, of course, relies on the State certification as to the correctness of the data, and we do not nor can we make any independent attempt to verify the information.

Each fall, before the beginning of the income tax filing season, HHS provides Internal Revenue with a consolidated nationwide listing of the persons who owe delinquent support payments, the amounts, and the States to which the payments are owed. The Internal Revenue then compares this information to the data in the individual master file accounts, and marks the accounts to be offset when and if a tax return is filed. When a return is processed against a marked file, any refund that is due is then offset—that is, reduced—by the amount of the delinquent support payment. At that time a notice is sent to the taxpayer advising him or her of the offset and the reason for it.

Obviously, the offset cannot exceed the amount of the refund, and the taxpayer receives any portion of the refund that remains after the offset has been satisfied.

In 1982, the first year of the program, Internal Revenue made some 279,000 offsets, with resulting revenues of about $174 million. In 1983, through August, we had made some 323,000 offsets, with resulting revenues of about $170 million which is just slightly less than last year. The average offset, therefore, has declined from about $624 in 1982 to about $526 so far this year.

In 1982 the Service was reimbursed by HHS at the rate of $17 per case, for about $4.7 million in total. In 1983 we are being reimbursed at $11 a case, which through August has amounted to $3.6 million in total. We anticipate a further decline in our cost per case next year. The Office of Management and Budget is aware of the reimbursable nature of this program and its impact on our budget.

We are still not certain what impact this program has or may have on the overall tax administration system or Federal revenue collections. Its relatively small size—fewer than 280,000 net offsets in 1982, compared to something over 71.6 million individual income tax refunds issued in that year—makes it pretty difficult to assess in relation to our total tax administration responsibilities.

We have, however, serious and continuing concerns about the program's potentially adverse impact on the tax system. These include the program's effect on withholding patterns, on cash flow to

the Treasury, and on our costs to collect tax revenues. In particular, we are concerned that taxpayers' filing and paying habits may be altered, once they have experienced the offset, leading to a greater number of filing delinquencies and unpaid balance-due accounts.

As you are aware, we are now engaged in a research effort to determine the impact this program may have had on tax administration, especially its effect on individual filing and withholding patterns, and ultimately on Federal revenues collected. The results of this study for this first year will be available sometime around the end of October.

Setting these potential problems aside, however, we have an equally pressing concern for the adverse publicity that we have received for our participation in the program. This has resulted from situations such as the following:

Incorrect data being received from the States, causing erroneous debtor certification;

Taxpayers not being notified by the States that an offset would be made, raising due process issues; and then finally,

Offsets being made on combined refunds on joint returns, adversely affecting spouses that are not obligated—we refer to them as nonobligated spouses.

While none of these problems are insurmountable in the long run, they certainly do concern us because of their potential impact on tax administration and our responsibilities. Voluntary compliance depends to a large degree on taxpayer perceptions that the system operates in a fair but firm manner. Any event that alters those perceptions has the potential at least to adversely affect voluntary compliance. And I know, Mr. Chairman, that you are well aware of the importance of voluntary compliance to the functioning of the system.

It is our belief that most taxpayers continue to proceed on the assumption that information they put on their tax returns is inviolate, and will not be pulled from the returns and used against them for some nontax matter. The fact that this program and others like it are authorized by Congress and entirely legal is of little consequence to those taxpayers; they still feel that somehow it violates their trust in the tax administration system. So this attitude, right or wrong, is a very real attitude.

Now, while those of us at IRS have learned to live with the knowledge that tax collection is probably the least popular function in Government, we have also come to believe that it is perhaps the most vital function, since obviously without the revenues that are so collected all other functions of Government would eventually come to a halt. We are always concerned when events beyond our control endanger the health of the tax system.

Mr. Chairman, I would like to conclude the direct testimony at this point by saying that we appreciate the opportunity to present our comments and to discuss this important topic. We are very interested in the statements that the other witnesses will be making here today. We will continue to operate this program to the best of our ability, consistent, of course, with sound tax administration. And once our research into the effects of this program on filing and withholding patterns, at least for the second year, is complete,

we will be in a much better position, we think, to evaluate its effect, or at least to give a good indication of the trends.

Now, Mr. Chairman, after Mr. Pearlman's statement we will be happy to answer whatever questions you may have.

Senator GRASSLEY. All right. Thank you.

Mr. Pearlman?

[Commissioner Egger's prepared statement follows:]

STATEMENT OF
ROSCOE L. EGGER, JR.
COMMISSIONER OF INTERNAL REVENUE
BEFORE THE
SUBCOMMITTEE ON OVERSIGHT OF THE INTERNAL REVENUE SERVICE
SENATE FINANCE COMMITTEE

SEPTEMBER 16, 1983

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

I AM PLEASED TO BE WITH YOU TODAY TO DISCUSS THE SERVICE'S PROGRAM TO COLLECT PAST-DUE CHILD AND SPOUSAL SUPPORT BY INCOME TAX REFUND OFFSET. IN MY TESTIMONY, I WILL BRIEFLY OUTLINE THIS PROGRAM, PROVIDE SOME EXAMPLES OF THE PROBLEMS ENCOUNTERED IN THE PROGRAM, AND REVIEW COURT DECISIONS ON THE PROGRAM AND THEIR IMPACT ON THE SERVICE.

WITH ME TODAY ARE SERVICE OFFICIALS FAMILIAR WITH VARIOUS ASPECTS OF THE PROGRAM. THEY WILL BE AVAILABLE TO ASSIST ME AS NEEDED IN RESPONDING TO ANY QUESTIONS YOU OR THE MEMBERS MAY HAVE.

IRS ADMINISTRATION OF THE PROGRAM

THE GOVERNMENT'S EFFORTS TO COLLECT PAST-DUE CHILD AND SPOUSAL SUPPORT FROM FEDERAL TAX REFUNDS WERE INSTITUTED AS PART OF PUBLIC LAW 97-35, THE OMNIBUS BUDGET RECONCILIATION ACT OF 1981. THE ACT, APPROVED IN AUGUST OF 1981 AND EFFECTIVE ON OCTOBER 1 OF THAT YEAR (THE START OF FISCAL YEAR 1982), PROVIDED IN GENERAL THAT INDIVIDUAL INCOME TAX OVERPAYMENTS (I.E., REFUNDS) MAY BE OFFSET TO THE EXTENT OF CERTAIN DELINQUENT CHILD AND SPOUSAL SUPPORT OBLIGATIONS. DATA ON THE INDIVIDUALS INVOLVED, THE EXISTENCE OF THESE OBLIGATIONS, AND THE AMOUNTS TO BE OFFSET ARE VALIDATED BY THE STATES AND SENT TO THE OFFICE OF CHILD SUPPORT ENFORCEMENT (OCSE) OF THE DEPARTMENT OF HEALTH AND HUMAN SERVICES (HHS). HHS THEN FORWARDS THIS INFORMATION TO THE SERVICE. WE BEGAN OFFSETTING REFUNDS UNDER THIS PROGRAM IN JANUARY 1982.

TO BETTER UNDERSTAND THE IRS' ROLE IN THIS PROGRAM, LET ME BRIEFLY DESCRIBE HOW A SAMPLE CASE WOULD WORK. FOR EASE OF DISCUSSION, I WILL USE A SIMPLE CASE, BUT YOU SHOULD BE AWARE THAT MANY OF THESE CASES ARE QUITE COMPLEX.

AN OBLIGATION FOR CHILD OR SPOUSAL SUPPORT ARISES FROM A COURT OR ADMINISTRATIVE ORDER, TYPICALLY AS A RESULT OF

A DIVORCE OR SEPARATION. WHEN AND IF THE SPOUSE WITH THE OBLIGATION FAILS TO MEET IT, THE OTHER SPOUSE -- WITH CUSTODY OF ANY CHILDREN -- MAY BE FORCED TO SEEK ASSISTANCE UNDER THE AID TO FAMILIES WITH DEPENDENT CHILDREN (AFDC) PROGRAM, WHICH IS FUNDED BY HHS AND ADMINISTERED BY THE STATES.

AS A CONDITION OF RECEIVING AFDC ASSISTANCE, THE SPOUSE MUST ASSIGN HIS/HER RIGHTS TO SUPPORT PAYMENTS TO THE WELFARE AGENCY OF THE STATE INVOLVED. THE STATE HAS AN OBLIGATION UNDER FEDERAL LAW TO VERIFY THAT THE INFORMATION ON THOSE PAYMENTS IS CORRECT AND TO TRY TO COLLECT THAT SUPPORT, AND AS PART OF THAT RESPONSIBILITY MUST REFER CERTAIN UNCOLLECTED CASES TO IRS (THROUGH HHS) ANNUALLY. THE SERVICE, OF COURSE, RELIES ON THE STATES' CERTIFICATION AS TO THE CORRECTNESS OF THE DATA, AND MAKES NO INDEPENDENT ATTEMPT TO VERIFY THE INFORMATION.

EACH FALL, BEFORE THE BEGINNING OF THE INCOME TAX FILING SEASON, HHS PROVIDES IRS WITH A CONSOLIDATED NATIONWIDE LISTING OF THE PERSONS WHO OWE DELINQUENT SUPPORT PAYMENTS, THE AMOUNTS, AND THE STATES TO WHICH THE PAYMENTS ARE OWED. IRS COMPARES THIS INFORMATION TO THE DATA IN ITS INDIVIDUAL MASTER FILE ACCOUNTS, AND MARKS THE ACCOUNTS TO BE OFFSET WHEN AND IF A TAX RETURN IS FILED. WHEN A RETURN IS PROCESSED AGAINST A MARKED FILE, ANY

REFUND DUE IS OFFSET (I.E., REDUCED) BY THE AMOUNT OF THE DELINQUENT SUPPORT PAYMENT. AT THAT TIME, A NOTICE IS SENT TO THE TAXPAYER ADVISING HIM/HER OF THE OFFSET AND THE REASON FOR IT.

OBVIOUSLY, THE OFFSET CANNOT EXCEED THE AMOUNT OF THE REFUND, AND THE TAXPAYER RECEIVES ANY PORTION OF THE REFUND REMAINING AFTER THE OFFSET.

IN 1982, THE FIRST YEAR OF THE PROGRAM, IRS MADE SOME 279,000 OFFSETS, WITH RESULTING REVENUES OF ABOUT $174 MILLION. IN 1983, THROUGH AUGUST, WE HAD MADE SOME 323,000 OFFSETS, WITH RESULTING REVENUES OF AROUND $170 MILLION. THE AVERAGE OFFSET HAS DECLINED FROM ABOUT $624 IN 1982 TO ABOUT $526 SO FAR IN 1983.

IN 1982, THE SERVICE WAS REIMBURSED BY HHS AT THE RATE OF $17 PER CASE, OR SOME $4.7 MILLION IN TOTAL. FOR 1983, WE ARE BEING REIMBURSED AT $11 PER CASE, WHICH THROUGH AUGUST HAS AMOUNTED TO ABOUT $3.6 MILLION IN TOTAL. WE ANTICIPATE A FURTHER DECLINE IN OUR COST PER CASE NEXT YEAR. THE OFFICE OF MANAGEMENT AND BUDGET IS AWARE OF THE REIMBURSEABLE NATURE OF THIS PROGRAM AND ITS IMPACT ON OUR BUDGET.

TAX ADMINISTRATION CONCERNS

WE ARE STILL NOT CERTAIN WHAT IMPACT THIS PROGRAM HAS HAD ON THE OVERALL TAX ADMINISTRATION SYSTEM OR FEDERAL REVENUE COLLECTIONS. ITS RELATIVELY SMALL SIZE, FOR EXAMPLE--FEWER THAN 280,000 NET OFFSETS IN 1982, COMPARED TO WELL OVER 71.6 MILLION INDIVIDUAL INCOME TAX REFUNDS ISSUED THAT YEAR--MAKES IT DIFFICULT TO ASSESS IN RELATION TO OUR TOTAL TAX ADMINISTRATION RESPONSIBILITIES.

WE HAVE, HOWEVER, SERIOUS AND CONTINUING CONCERNS ABOUT THE PROGRAM'S POTENTIALLY ADVERSE IMPACT ON THE TAX SYSTEM. THESE INCLUDE THE PROGRAM'S EFFECT ON WITHHOLDING PATTERNS, ON CASH FLOW TO THE TREASURY, AND ON OUR COSTS TO COLLECT TAX REVENUES. IN PARTICULAR, WE ARE CONCERNED THAT TAXPAYERS' FILING AND PAYING HABITS WILL BE ALTERED ONCE THEY'VE EXPERIENCED AN OFFSET, LEADING TO A GREATER NUMBER OF FILING DELINQUENCIES AND UNPAID BALANCE DUE ACCOUNTS.

AS YOU ARE AWARE, HOWEVER, WE ARE NOW ENGAGED IN RESEARCH TO DETERMINE THE IMPACT THIS PROGRAM MAY HAVE HAD ON TAX ADMINISTRATION, ESPECIALLY ITS EFFECT ON INDIVIDUAL FILING AND WITHHOLDING PATTERNS, AND ULTIMATELY ON FEDERAL REVENUES COLLECTED. THE RESULTS OF THIS STUDY SHOULD BE AVAILABLE SOMETIME AROUND THE END OF OCTOBER.

SETTING THESE POTENTIAL PROBLEMS ASIDE, WE HAVE AN EQUALLY PRESSING CONCERN FOR THE ADVERSE PUBLICITY RECEIVED FROM OUR PARTICIPATION IN THIS PROGRAM. THIS HAS RESULTED FROM SITUATIONS SUCH AS THE FOLLOWING:

- O INCORRECT DATA BEING RECEIVED FROM THE STATES, CAUSING ERRONEOUS DEBTOR CERTIFICATION, ETC.;
- O TAXPAYERS NOT BEING NOTIFIED BY THE STATES THAT AN OFFSET WOULD BE MADE, RAISING DUE PROCESS ISSUES; AND
- O OFFSETS BEING MADE ON COMBINED REFUNDS ON JOINT RETURNS, ADVERSELY AFFECTING NONOBLIGATED SPOUSES.

WHILE NONE OF THESE PROBLEMS ARE INSURMOUNTABLE IN THE LONG RUN, THEY CONCERN US BECAUSE OF THEIR POTENTIAL IMPACT ON OUR TAX ADMINISTRATION RESPONSIBILITIES. VOLUNTARY COMPLIANCE DEPENDS TO A LARGE DEGREE ON TAXPAYERS' PERCEPTIONS THAT THE SYSTEM OPERATES IN A FAIR BUT FIRM MANNER. ANY EVENT THAT ALTERS THOSE PERCEPTIONS HAS THE POTENTIAL TO ADVERSELY AFFECT VOLUNTARY COMPLIANCE, AND I KNOW YOU ARE WELL AWARE, MR. CHAIRMAN, OF THE IMPORTANCE OF VOLUNTARY COMPLIANCE TO THE FUNCTIONING OF THE TAX SYSTEM.

IT IS OUR BELIEF THAT MOST TAXPAYERS PROCEED ON THE ASSUMPTION THAT THE INFORMATION ON THEIR TAX RETURNS IS INVIOLATE, AND WILL NOT BE PULLED FROM THEIR RETURNS AND USED AGAINST THEM IN A NON-TAX MATTER. THE FACT THAT THIS PROGRAM, AND OTHERS LIKE IT, ARE AUTHORIZED BY CONGRESS AND ENTIRELY LEGAL IS OF LITTLE CONSEQUENCE TO THESE TAXPAYERS; THEY STILL FEEL IT SOMEHOW VIOLATES THEIR TRUST IN THE TAX ADMINISTRATION SYSTEM. THIS ATTITUDE, RIGHT OR WRONG, IS VERY REAL.

WHILE THOSE OF US AT IRS HAVE LEARNED TO LIVE WITH THE KNOWLEDGE THAT TAX COLLECTION IS PERHAPS THE LEAST POPULAR FUNCTION OF GOVERNMENT, WE HAVE ALSO COME TO BELIEVE THAT IT IS PERHAPS THE MOST VITAL FUNCTION, SINCE WITHOUT THE REVENUES SO COLLECTED ALL OTHER FUNCTIONS OF GOVERNMENT WOULD EVENTUALLY COME TO A HALT. WE ARE ALWAYS CONCERNED WHEN EVENTS BEYOND OUR CONTROL ENDANGER THE HEALTH OF THE TAX ADMINISTRATION SYSTEM.

LEGAL PROBLEM AREAS

THERE HAVE BEEN SEVERAL COURT DECISIONS RENDERED ON LEGAL CHALLENGES TO THE OFFSET PROGRAM. THE MOST COMMON AREA OF CONCERN TO BE CHALLENGED IS DUE PROCESS.

THE DUE PROCESS CONCERN HAS CENTERED PRINCIPALLY ON THE SITUATION OF THE SPOUSES OF TAXPAYERS WHO ARE INDEBTED FOR CHILD AND/OR SPOUSAL SUPPORT BY REASON OF A PRIOR MARRIAGE OR PATERNITY ORDER. THE CURRENT SPOUSES OF DELINQUENT INDIVIDUALS ARE THEMSELVES NOT LIABLE FOR SUPPORT, NONETHELESS, A REFUND DUE TO A DELINQUENT INDIVIDUAL AND HIS OR HER CURRENT SPOUSE IS SUBJECT TO OFFSET.

THE SERVICE ACKNOWLEDGES THAT THE CURRENT NONLIABLE OR "NONOBLIGATED" SPOUSE MAY HAVE A SEPARATE INTEREST IN A REFUND APPEARING ON THE TAXPAYERS' JOINT RETURN BECAUSE OF THE NONLIABLE SPOUSE'S SEPARATE EARNINGS OR SHARE OF AN EARNED INCOME CREDIT OR OTHER TAX CREDIT. NEVERTHELESS, THE LAW VERY SPECIFICALLY REQUIRES THE OFFSET PROCESS TO OPERATE AGAINST TAXPAYERS OWING PAST-DUE SUPPORT "REGARDLESS OF WHETHER SUCH INDIVIDUAL FILED A TAX RETURN AS A MARRIED OR UNMARRIED INDIVIDUAL . . . ." (42 U.S.C. SEC. 664). THUS THE PORTION OF A REFUND DUE TO THE NONOBLIGATED SPOUSE MAY BE SUBJECT TO OFFSET.

THE SERVICE HAS FROM THE BEGINNING OF THE CHILD SUPPORT OFFSET PROGRAM RECOGNIZED THAT THE NONLIABLE SPOUSE MAY CLAIM HIS OR HER SHARE OF A REFUND OFFSET UNDER THE PROGRAM, AND THE SERVICE WILL ALLOCATE THE NONLIABLE SPOUSE'S CORRECT SHARE AND MAKE THE PROPER REFUND; BUT IT

IS NECESSARY FOR NONLIABLE SPOUSES TO FIRST FILE CLAIMS TO GET THEIR SHARE OF THE OFFSET REFUND, SINCE WITHOUT A CLAIM THE SERVICE LACKS SUFFICIENT INFORMATION TO ALLOCATE AN OVERPAYMENT ON A JOINT RETURN.

DESPITE THE SERVICE'S RECOGNITION OF THE RIGHT OF NONLIABLE SPOUSES TO ALLOCATION OF THE INTERCEPTED REFUND, MANY OF THE LAWSUITS BROUGHT AGAINST THE PROGRAM HAVE CONTENDED THAT THE INITIAL OFFSET AGAINST THE ENTIRE OVERPAYMENT ON A JOINT RETURN VIOLATES THE NONLIABLE SPOUSE'S FIFTH AMENDMENT RIGHT NOT TO BE DEPRIVED OF PROPERTY WITHOUT DUE PROCESS OF LAW.

IN SORENSON V. SECRETARY OF THE TREASURY, 557 F. SUPP. 729 (1982), THE DISTRICT COURT FOR THE WESTERN DISTRICT OF WASHINGTON ORDERED THE SERVICE TO ADD TO THE STATUTORY NOTICE OF OFFSET ADDITIONAL INFORMATION TO INFORM NONLIABLE SPOUSES OF THE RIGHT TO CLAIM A SHARE OF THE OVERPAYMENT. (HERE, THIS WAS HELD TO BE ONE-HALF OF THE OVERPAYMENT, SINCE WASHINGTON IS A COMMUNITY-PROPERTY STATE. THE SERVICE'S PROBLEMS WITH NONLIABLE SPOUSES ARE ONLY EXACERBATED BY THE COMMUNITY PROPERTY LAWS.) THIS CHANGE IN THE NOTICE WAS A STEP THE SERVICE WAS ALREADY IN THE PROCESS OF IMPLEMENTING. IN THE PAST YEAR'S PROGRAM (THE 1983 PROGRAM INVOLVING 1982 TAX RETURNS), ALL NOTICES OF RETAINED REFUNDS HAVE CONTAINED INFORMATION INFORMING

THE NONLIABLE SPOUSE OF HIS OR HER RIGHT TO FILE A CLAIM. THE COURT IN SORENSON STATED: "BESIDES ADEQUATE NOTICE, NO ADDITIONAL PROCEEDINGS ARE REQUIRED BY DUE PROCESS."

IT IS SIGNIFICANT TO NOTE THAT IN THE SORENSON CASE, THE DISTRICT COURT RULED THAT DUE PROCESS DOES NOT REQUIRE THE FEDERAL GOVERNMENT TO HOLD A HEARING ON THE AMOUNT DUE FOR CHILD SUPPORT OR ON THE TAXPAYER'S ABILITY TO PAY. SUCH RELIEF, AS INDICATED IN THE COURT'S OPINION, IS APPROPRIATELY LEFT TO STATE PROCEEDINGS AT WHICH FACTUAL DEFENSES TO THE SUPPORT OBLIGATION MAY BE RAISED.

IN THE OTHER REPORTED CASE TO REACH THE MERITS OF THE DUE PROCESS ISSUE, NELSON V. REGAN 560 F. SUPP. 1101 (D. CONN. 1983), A SOMEWHAT DIFFERENT--BUT CONSISTENT--RESULT WAS REACHED. IN ITS JANUARY 14, 1983 RULING, THE DISTRICT COURT RULED THAT THE STATE OF CONNECTICUT WAS OBLIGATED, AS A REQUIREMENT OF DUE PROCESS, TO PROVIDE INDIVIDUALS ALLEGED TO OWE PAST-DUE SUPPORT WITH A DETAILED NOTICE SPELLING OUT POSSIBLE DEFENSES TO LIABILITY, THE PROCEDURES FOR ASSERTING SUCH DEFENSES BEFORE THE DEBT COULD BE REFERRED TO THE FEDERAL GOVERNMENT, AND A PRE-OFFSET ADMINISTRATIVE HEARING ON THE DEFENSES RAISED.

AS FAR AS THE FEDERAL GOVERNMENT IS CONCERNED, HOWEVER, THE NELSON COURT IN ITS APRIL 22, 1983, "RULING ON REMEDY AND FINAL ORDER" HELD THAT THE INTERNAL REVENUE SERVICE WAS NOT RESPONSIBLE FOR PRE-OFFSET ALLOCATION OF THE NONLIABLE SPOUSE'S SHARE OF THE REFUND. AGAIN, ADEQUATE NOTICE TO THE NONLIABLE SPOUSE OF THE RIGHT TO CLAIM HIS OR HER APPROPRIATE SHARE OF THE REFUND IS ALL THAT DUE PROCESS REQUIRES OF THE FEDERAL GOVERNMENT. DESPITE THE COURT'S RULING THAT A SEPARATE NOTICE BE SENT TO THE NONLIABLE SPOUSE, THE COURT LATER ACCEPTED THE PARTIES' STIPULATION THAT A JOINT NOTICE TO THE OBLIGATED AND NONOBLIGATED SPOUSE IS SUFFICIENT. AS I PREVIOUSLY POINTED OUT, THIS IS THE TYPE OF NOTICE THAT THE SERVICE NOW SENDS.

YOU SHOULD BE AWARE, HOWEVER, THAT BOTH SORENSON AND NELSON ARE PRESENTLY BEING APPEALED TO THEIR RESPECTIVE CIRCUITS.

CONCLUSION

MR. CHAIRMAN, WE APPRECIATE THE OPPORTUNITY TO PRESENT OUR COMMENTS ON THIS IMPORTANT TOPIC, AND ARE VERY INTERESTED IN THE STATEMENTS OF THE OTHER WITNESSES HERE TODAY.

WE WILL CONTINUE TO OPERATE THIS PROGRAM TO THE BEST OF OUR ABILITY, CONSISTENT WITH SOUND TAX ADMINISTRATION. ONCE OUR RESEARCH INTO THE EFFECTS OF THIS PROGRAM ON FILING AND WITHHOLDING PATTERNS IS COMPLETE, WE WILL BE IN A MUCH BETTER POSITION TO EVALUATE ITS EFFECT ON FEDERAL REVENUES COLLECTED.

MY ASSOCIATES AND I WILL BE PLEASED TO TRY AND ANSWER ANY QUESTIONS YOU OR THE MEMBERS MAY HAVE.

STATEMENT OF RONALD A. PEARLMAN, DEPUTY ASSISTANT SECRETARY, TAX POLICY, DEPARTMENT OF THE TREASURY, WASHINGTON, D.C.

Mr. PEARLMAN. Thank you, Mr. Chairman. I am pleased to be here this morning with Commissioner Egger.

Our responsibility is to offer the Treasury's views on S. 150, which would establish a new collection procedure for student loans in default.

For the reasons that I will discuss and that are contained in my written statement, the Treasury Department is opposed to S. 150 at this time.

Under current law there is no procedure for involving the tax collection process in the collection of defaulted student loans. As Mr. Egger has described by analogy, the Code does provide a procedure for offsetting past-due child support payments against overpayments of tax, the so-called tax refund offset procedure, and in the case of student loans the Internal Revenue Code does currently require the Internal Revenue Service to disclose to the Department of Education the mailing address of any taxpayer who has defaulted on a loan made under several student loan programs.

But S. 150 would, for the first time, make the tax collection process beyond simply refund offset available for the collection of nontax items, specifically certainly defaulted student loans. It would require obligors in default to pay their defaulted obligation at the time they file their tax returns, and it would require the Internal Revenue Service to use its affirmative collection procedures, including jeopardy assessment authority, to collect unpaid amounts as if they were taxes.

Under the bill, specifically, each calendar quarter the Department of Education would provide the Internal Revenue Service with the name and last known address and the amount due on a defaulted obligation, which category of obligations are those student loans made, insured, or guaranteed under part B of title IV of the Higher Education Act of 1965.

The Service would then be required to promptly notify the obligor of the default and describe to the obligor the precedures for payment. If there is a refund, the Service would be required to offset the refund. If there is no refund, the Service would be required to collect the amount due, and that would include the normal assessment process—notice, demand for payment, and then, as I mentioned before, the various levy procedures that are available to the Revenue Service, including the jeopardy assessment procedure.

We recognize and are sympathetic to the need to improve collection of delinquent student loans, and indeed other Federal debts; but nevertheless, at this time we must oppose S. 150.

As Commissioner Egger indicated in his statement this morning, the Service is currently in the process of analyzing the cost and effectiveness of the child support offset program, but we think it would be premature to conside extending the use of offsets, and then to go beyond that and make applicable the general collection procedures to nontax debts until the results of that analysis are known.

This analysis is currently in process, pursuant to a decision of the Cabinet Council on Economic Affairs, and we think that the ability to evaluate all of these collection processes will be much better after that analysis is completed.

We, as the Commissioner, are very concerned about the direct and indirect costs to the tax system of using both refund offset procedures and affirmative collection procedure as a collection mechanism for Federal debts.

Our strongest concern involves the public reaction that the Commissioner referred to, in using the system for the collection of a nontax debt. Taxpayers become indebted to the Federal Government in a number of ways, and any broad scale use of the tax system to collect debts owed in connection with these programs may detract from the collection efforts that are the direct responsibility and the immediate responsibility of the Service in connection with taxes. And we certainly want to make sure that does not happen.

There is no concrete evidence to date that indicates that taxpayers who are subject to refund offset will manipulate their withholding and estimated taxes, but we are concerned by that possibility, and we hope that the analysis that I referred to a moment ago will help us in evaluating that possibility.

But certainly we do not want to put taxpayers in a position where they are encouraged to reduce their withhold and create balance-dues that otherwise would not occur, or indeed a possibility that certain taxpayers would not file their tax returns.

We would also point out that under S. 150 the full cost of providing this collection service, if you will, would be borne by the Internal Revenue Service, and we think in general terms, as a general rule, that is not wise, that does not permit a proper allocation of the costs of any Federal program to the proper Federal agency. And we think the more appropriate approach would be to identify the collection expenses that the Service would be incurring to the particular program, as distinguished from having them hidden in the budget of the Service.

Finally, we would hope that the subcommittee would keep in mind the issues that can arise when a debt collector, if you will, is not the same, doesn't have the same identity, as the creditor.

When the Service is required to collect taxes for which it has full administrative responsibility, it also has the ability to make judgments about the specific collection procedures it wishes to utilize and the timing of the exercise of those procedures. Put simply and most straightforwardly, the Service can exercise some of the human judgment that we really want the Service to exercise in dealing with taxpayers.

When the creditor is someone other than the collection agent, as would be the case under S. 150, the Service might be placed in a position where it has to enforce its collection remedies on a more mechanical basis—that is, to collect an unpaid obligation at all costs. This problem is not nearly so serious with a refund offset procedure as it is when we talk about the extraordinary remedies the Service has available, such as jeopardy assessment and levy.

We think that over the years the Service has exercised commendable judgment in using its various statutory collection au-

thorities, and we hope that we would all agree that the Service would be entitled to exercise that same judgment in connection with any other collection responsibilities given to it by the Congress.

For the above reasons, we must oppose S. 150 at this time, but we are certainly happy to continue to work with the subcommittee and our sister agencies in trying to deal with what we acknowledge to be a serious collection problem.

Mr. Chairman, this concludes my prepared remarks. I will be happy to join the Commissioner in seeking to answer your questions.

Thank you.

[The prepared statement of Hon. Ronald A. Pearlman follows:]

28-099 O - 84 - 3

For Release Upon Delivery

Expected at 9:30 a.m. EDT
September 16, 1983

STATEMENT OF
RONALD A. PEARLMAN
DEPUTY ASSISTANT SECRETARY (TAX POLICY)
DEPARTMENT OF THE TREASURY
BEFORE THE
SUBCOMMITTEE ON OVERSIGHT OF THE
INTERNAL REVENUE SERVICE
OF THE
SENATE COMMITTEE ON FINANCE

Mr. Chairman and Members of the Subcommittee:

I am pleased to have the opportunity to present the views of the Treasury Department on S. 150, which would establish a new collection procedure for student loans in default. For the reasons I will discuss, the Treasury Department is opposed to S. 150 at this time.

Background

Section 6402(a) of the Internal Revenue Code provides that the Internal Revenue Service is to refund any overpayment of tax to the person who made the overpayment after applying the overpayment to any other outstanding liability for tax owed by that person or for interest on such tax. Section 6402(c), enacted in 1981, provides an exception to this general rule whereby the IRS, in certain cases, is required to offset amounts of past-due child and spousal support against the amount of any tax overpayment that otherwise would be refunded to the person who owes this support. Tax refunds that are offset under this procedure are remitted by the Internal Revenue Service to a special account maintained by the Bureau of Government Financial

Operations for distribution to the States. Section 6305(a) requires the IRS to assess and collect an amount which has been certified by the Department of Health and Human Services as the amount of a delinquent child and spousal support payment determined under a State court order or an order of an administrative process established under State law, as if such amount were an employment tax the collection of which would be jeopardized by delay.

No similar offset provision is provided for the collection of defaulted student loans or other nontax liabilities. However, section 6103(m)(4) requires the IRS to disclose to the Department of Education the mailing address of any taxpayer who has defaulted on a loan made under various Federal student loan programs.

Description of S. 150

S. 150 generally would establish a procedure whereby taxpayers who are in default on certain student loans must satisfy their obligation for payment when they file their Federal income tax returns. The bill also would give the Internal Revenue Service jeopardy assessment authority in cases where payment is not made in accordance with this procedure. Specifically, the bill would require the Department of Education, at the end of each calendar quarter, to provide the Internal Revenue Service with the name of each borrower who has defaulted on a student loan made, insured or guaranteed under part B of title IV of the Higher Education Act of 1965. The transmittal is to include the name and last known address of the borrower, the amount of the unpaid principal and accrued interest with respect to each loan and the name of the holder of each loan.

No later than 15 days after the close of the taxable year (January 15 in the case of all calendar year taxpayers), the IRS is to notify each defaulting borrower of the provisions of the new law and to advise that he is to make payment of the outstanding principal and accrued interest on each defaulted loan when he files his tax return for the prior taxable year. The Service is authorized to provide rules for payment in cases where an extension of time for filing a return is granted or where no return is required to be filed. The notice is to be mailed to the borrower's last known address or left at his dwelling or usual place of business.

In addition, the bill would authorize the Internal Revenue Service to reduce any overpayment of tax to be refunded to a taxpayer by the amount of the loan and interest in default. In cases where there is no refund or the refund is insufficient to cover the amount owed and the borrower fails to make a timely payment of the full amount owed, the Service is required to collect the amount in the same manner as if it were making a jeopardy assessment of an employment tax. Thus, the Service would be authorized to make an immediate assessment and immediate notice and demand for payment of the overdue amount. Further, upon the borrower's failure or refusal to pay that amount, the Secretary would be authorized to collect the amount by levy, without regard to any otherwise applicable waiting period.

Discussion

While we recognize the need to improve collection methods for delinquent student loans and other Federal debts, the Treasury Department opposes S. 150. As Commissioner Egger indicated in his statement this morning, the Service is currently analyzing the costs and effectiveness of the existing child support offset provision. We believe it would be premature to consider expanding the use of offsets at least until the results of that analysis are known. Any further use of the tax system for collection of nontax debts should be undertaken only after a most thorough analysis of the considerations involved. This analysis is currently in progress pursuant to a decision by the Cabinet Council on Economic Affairs.

The Treasury Department is concerned about the direct and indirect costs to the tax system of using refund offsets as a collection mechanism for Federal debts. Our strongest concern involves the public's reaction to using the tax system for collection of a nontax debt. Taxpayers become indebted to the Federal government in many ways, and any broadscale use of the tax system to collect debts owed in connection with these Federal programs may detract from regular collection efforts and could have troublesome implications.

While there is no concrete evidence to date to suggest that taxpayers who are subject to the offset procedure will eventually adjust their withholding and estimated tax payments to avoid any tax overpayments or indeed chose not to

file a tax return at all, we are concerned that individuals may reduce their withholding. Should this occur, it would increase the "balance due" returns and delinquent accounts that require increased IRS collection efforts. We will adress this question in connection with our assessment of the existing child support offset provision.

Additionally, under S. 150, the full cost of providing notice to borrowers in default, as well as the cost of collecting the delinquent amounts, is to be borne by the Internal Revenue Service. As a general rule, we believe that each Federal agency should bear such costs. Otherwise, there will be no practical way to evaluate the budget of each program. The costs of a particular program, including debt collection, cannot be accurately determined if they are hidden in the budget of the Internal Revenue Service.

For these reasons, Treasury must oppose S. 150 at this time.

This concludes my prepared remarks. I would be happy to answer your questions.

Senator GRASSLEY. A general question for clarification as far as your testimony, Mr. Pearlman: Were any of your statements applicable also to the principle of extending the tax offset to nonwelfare families in the case of child support? Or is your testimony directed totally toward S. 150?

Mr. PEARLMAN. Well, our testimony is directed—our written statement, and indeed my oral comments were intended toward S. 150, but I think there are analogous concerns that really the Commissioner expressed in connection with the refund offset procedures.

Senator GRASSLEY. Commissioner, the report you said that would be available, I think the last of October.

Commissioner EGGER. Yes; what we are doing is attempting to analyze these accounts as to their effect on tax collections.

Senator GRASSLEY. To see if there is any adverse impact on tax collection?

Commissioner EGGER. To see if we can detect trends with respect to any adverse impact on collection, to see what is happening to withholding patterns, and that kind of thing.

Senator GRASSLEY. To see if it is impacting on voluntary compliance?

Commissioner EGGER. Right.

Senator GRASSLEY. And that report will be ready the last of October?

Commissioner EGGER. We expect to have the analysis finished by about that time.

Senator GRASSLEY. Would it be available to us, then, about that same time?

Commissioner EGGER. I feel certain we could make it available to you.

Senator GRASSLEY. I think it would be good if we could have that just as soon as you have it compiled.

Commissioner EGGER. Sure.

Senator GRASSLEY. I suppose compiled or printed or whatever you are going to do.

Commissioner EGGER. I don't know if we are going to make a public release of it, Mr. Chairman.

Senator GRASSLEY. But we could have access to the summaries and conclusions?

Commissioner EGGER. Yes.

One of the problems that I have with it is that it will be interpreted as being sort of set in concrete. My own personal view is that, although we can probably detect some trends, we do have to keep in mind that patterns of this type develop over much longer periods, and it would probably be risky to try to draw too many final conclusions on the basis of only this 1 year of experience.

Senator GRASSLEY. OK. Well, we would realize that we would have to treat it with caution.

Mr. Egger, in 1975 Congress gave the IRS the authority to collect delinquent child support enforcement accounts as it collected delinquent taxes. Have you ever received requests to collect delinquent child support accounts?

Commissioner EGGER. We did—just a handful. And the explanation of that, as near as I understand it, and maybe Mr. Goldberg can add a bit more to it, was that, first off, the cost of actual field collection was so significant that for the most part it was not cost effective for the State agencies to incur that kind of cost. So we only had about 200 cases referred to us in the course of an average year.

Another reason of course, was that HHS had to certify under this earlier law, and since the State agencies themselves really have the facts and the details on the cases, it became both costly and difficult for HHS to certify.

The former law really wasn't doing much good anywhere as near as I could tell. So in 1981 when this issue came up, we sat down with HHS and the OMB and reviewed the possibility of moving into a strict refund offset approach. We expressed the concerns then that I have outlined here today, but concluded that certainly we were willing to make a try, to see what impact it does have.

Now, from where I view the matter at this time, the number of cases involved in actual refund offsets is such a small part of the whole refund universe that it probably will not have a major impact. Any attempt that we might make to analyze that in terms of a massive amount of cases of this sort, expanded into other areas, and so on—it's just extremely difficult to make that kind of a prediction.

Senator GRASSLEY. Out of those 150 cases, do you know whether any of them were pursued and collected upon?

Commissioner EGGER. I'm sure they were. Stan?

Mr. GOLDBERG. I believe they were, Senator. I don't have the numbers here. They were obviously very small numbers as compared to the offset.

Commissioner EGGER. But I feel certain that we did in fact collect some of them.

Senator GRASSLEY. OK.

Do you have the same similar concerns, with extending the refund offset concept in S. 150 as you do with the original child support enforcement refund offset program?

Commissioner EGGER. I do, until we can get a better feel for what the overall impact is going to be and how that impact might change or be altered as we expand the universe.

As I said before, the relatively small numbers here—even though we actually process some 800,000 cases this year—the relatively small numbers are not going to have that kind of impact, in my judgment.

Senator GRASSLEY. Would you repeat for me the statement in your testimony as to how much time and money is spent by the IRS to administer the current refund offset program?

Commissioner EGGER. Yes; let me give you those statistics:

In 1982, the cases that were referred to us by HHS were 547,000 cases. So far in 1983, and this is through August of 1983, we have had 821,000 referred to us. It is a significant increase there.

Of the cases that were actually identified for offset—and these are where we had an identity on the master file, 473,000 in 1982; 706,000 in 1983. But the cases that were actually offset were 279,000 in 1982, and 323,000 in 1983. So, as you can see, the numbers of actual offsets in comparison to the total cases referred to us is getting smaller.

The cost that we refer to HHS and for which we are reimbursed was $4.7 million last year on the cases that we handled. This year it is only $3.6 million.

Our staff year expenditure—this is the people power—158 staff years in 1982, and only 131 staff years in 1983. The reason for our lower cost and lower staff year effort is because a good bit of the processing in 1982 was manual, and we have since had time to program our systems and do a lot of this through the use of technology. We think that next year we will come down even some more on the cost of it.

Senator GRASSLEY. So then I presume you have a yearly review of the costs to the States. And are you somewhat sure that you are billing the States for the accurate amount of money, your costs?

Commissioner EGGER. The way we handle this is to give HHS a report on the dollars collected by State, and our costs. We set up the costs on a per-case basis, and we give them the number of cases by State as well as the dollars by State. So the State agencies are, in effect, bearing the costs, and they get the net amount of the refund offsets.

Senator GRASSLEY. Do you bill to include lost staff time?

Commissioner EGGER. Well, yes; the $4.7 million which HHS paid us last year, and the $3.6 million this year, is to reimburse us for our costs—that is, the staff time costs. Yes, sir.

Senator GRASSLEY. This figure also includes staff time,?

Commissioner EGGER. Well, right. That is part of the cost.

Senator GRASSLEY. OK.

Commissioner EGGER. Now, we don't have identified in our current budget specific staff year allocations for this effort. That is simply gleaned out of the total staff year allotments, and if it continues to grow obviously we have to reconsider our budget from that standpoint.

Senator GRASSLEY. Can you estimate how much your agency costs will increase, if at all, if you are required to offset refunds for non-AFDC dealings with parents?

Commissioner EGGER. We could give you an estimate if we knew what that universe is, but when we started out with this program, the HHS estimates were somewhere around 200-300,000 cases, and as you can see, this year we had 821,000 cases. So we don't know what the universe is. Therefore it is impossible for us to make a judgment as to what the cost will be. But it will be on a per-case basis. My guess is that it will be something less than the $11 per case that we have incurred this year.

Senator GRASSLEY. Are there any changes that the Congress ought to consider to simplify and expedite the current refund offset procedures?

Commissioner EGGER. At the moment we have pretty well resolved most of the problems that cropped up in the early stages here, the principal one being, of course, how do we deal with the nonobligated spouse? This is a case where the debtor spouse has remarried, and the nonobligated spouse has an interest in the refund. So what we are doing is inviting those people to apply for a refund and give us the information which will permit us to allocate the refund on some rational basis.

The due process issues, and so on—we have had a couple of court cases on those, and so they are pretty well resolved.

Senator GRASSLEY. Will this procedure satisfy the Sorenson Case?

Commissioner EGGER. Oh, I think so. Yes.

Senator GRASSLEY. OK.

Mr. GOLDBERG. I think so, too, Senator.

Senator GRASSLEY. Will you bill the State for the additional expense to satisfy the due-process requirements?

Commissioner EGGER. Yes; well, that's included in our overall cost. That is simply spread on a per-case cost basis.

I must say, Mr. Chairman, that we are being reimbursed for our costs in the program. This is not costing us out of pocket from our other budget allocations.

Senator GRASSLEY. I think my last question will be answered by this report, that we can share that information with you when that comes out the last of October.

Commissioner EGGER. Yes; I think it would be useful to review that with you. We aren't sure just what we are going to learn from that, but we have said in discussions of this particular issue over and over again with other agencies, OMB and so on, that we regard as an absolute essential that there be a fully effective pilot program that goes on and goes through an appropriate test period before this thing gets expanded; because if you expand it first and then learn the conclusions later, we think that that is inviting difficulties.

Senator GRASSLEY. Would you be as dogmatic as Mr. Pearlman was in his statement in which he said there is no evidence, to this point, that it does affect voluntary compliance, but that he does have concern that any——

Commissioner EGGER. I think what we are saying is that we are neutral at this point. We really can't say with any specificity what

the impacts are. Now, some of these impacts are going to be very difficult to measure, such as taxpayer perceptions.

Again, as I said, each time something of this sort comes up, the adverse publicity has some kind of an impact; but we don't know how to measure that.

Senator GRASSLEY. Mr. Pearlman also said that there wasn't any evidence that this affected the exemptions that people claim. So, you just don't know, the same way.

Commissioner EGGER. I am hopeful that the studies that we will conclude somewhere toward the end of October will give us some indication of that.

Senator GRASSLEY. Well, then I will ask my staff and the Joint Committee staff to get with your people soon after October 31 on that point.

Commissioner EGGER. Surely.

Senator GRASSLEY. Mr. Pearlman, I have a question about the legality of the provisions that relate to the fact that child support payments for non-AFDC families are not Federal debt problems, you already referred to that issue in your testimony, in conjunction with the educational loan program.

Would that in any way affect the legality, I suppose our constitutional ability to collect for non-AFDC families?

Mr. PEARLMAN. Mr. Chairman, I wouldn't want to answer that definitively, but there is some precedent for Federal Government collection of non-Federal Government debts, in the State income tax collection procedure, which I don't think is used by any State.

I would think that the Federal Government could, by legislation, authorize collection of a non-Federal Government debt. I wouldn't want to be held to that response, but I think there is some precedent for it; although, as I said, I don't think it has ever been used in the State income tax area.

Senator GRASSLEY. From strictly a political standpoint, let me clarify a point. You did state your opposition to S. 150, didn't involve the offset provisions. You are basically concerned about the extension of the income tax collection machinery of IRS to collect those education debts?

Mr. PEARLMAN. Well, let me just make sure that S. 150 does involve refund offsets in the case of student loans.

Senator GRASSLEY. Yes.

Mr. PEARLMAN. So in our statement that we are opposing 150, and specifically at this time, we are saying we think we should not go beyond child support refund offset until at least the Commissioner's study is completed.

Senator GRASSLEY. The reason I was curious is, there is some disagreement on our staff whether or not the income offset provisions were in S. 150.

Mr. PEARLMAN. Well, I think they are. We will stand corrected if we're incorrect.

Senator GRASSLEY. Our staff is saying it's a direct assessment and not an income offset.

Mr. PEARLMAN. It is clearly a direct assessment provision in S. 150, but in addition to that, the Service is directed to offset refunds. I am reasonably confident of that.

Senator GRASSLEY. Well, we can settle that later on. It doesn't have to be right now.

Mr. PEARLMAN. I think I'm correct.

Senator GRASSLEY. Let's forget about S. 150 now. The administration's bill on child support recovery affects non-welfare families, non-AFDC families. You aren't stating an Administration opposition to that concept?

Mr. PEARLMAN. No.

Senator GRASSLEY. No. OK.

Well, I guess along that very same line, I would like to ask you, then, your view on whether or not the present refund offset should be expanded to include non-AFDC families from the standpoint of the position of the Treasury Department.

Mr. PEARLMAN. I think we share the concern that the Commissioner expressed. I guess we would say the same thing, that we are a bit neutral on extending refund offset programs at this time, but we are most interested in the results of the analysis that the Service is going through. We are really talking about behavioral evaluation of these programs. We hope that we will all have some opportunity to do some careful review of the current program before we commit one way or the other on the extension of the refund offset program to the non-AFDC.

But I think it would be premature to be categorical in support or opposition, when we are only talking 60 days or so from having a bit more helpful information, if not more definitive information.

Senator GRASSLEY. OK. I think that takes care of the questions that I wanted to ask each one of you.

Did you, Mr. Goldberg, have anything you wanted to fill in here?

Mr. GOLDBERG. No, sir; the Commissioner covered it quite well.

Senator GRASSLEY. I want to thank all of you for your testimony. Thank you very much.

Mr. GOLDBERG. Thank you.

Commissioner EGGER. Thank you, Mr. Chairman.

Senator GRASSLEY. I might suggest not only to you but to any other witness that, because I'm the only one of the committee that probably will be able to be here today, that you may receive questions in writing from other members of the committee or from me, even, as a followup, and we would appreciate any response from not only the administration but any of the other witnesses. It would be helpful if those be responded to as quickly as possible. And the record will be open for 15 days, as well, to receive testimony from anybody who wasn't invited to testify, as well as anybody who has any additions or corrections to any of the testimony that might be given today.

Our next witness is from the Department of Health and Human Services, Mr. Fred Schutzman. He is Deputy Director of the Office of Child Support Enforcement. He has previously served as the Associate Commissioner in several offices of the Social Security Administration. He holds a bachelors degree from Cooper Union College in New York City and a masters degree from Columbia University, and I would appreciate it very much if you would introduce your associate.

Mr. SCHUTZMAN. Thank you, Mr. Chairman.

Accompanying me today is Mary Goeddes, Deputy Assistant Secretary for Legislation, of the Department.

STATEMENT OF FRED SCHUTZMAN, DEPUTY DIRECTOR, OFFICE OF CHILD SUPPORT ENFORCEMENT, DEPARTMENT OF HEALTH AND HUMAN SERVICES, WASHINGTON, D.C.

Mr. SCHUTZMAN. With your permission, Mr. Chairman, I would like to submit my full statement for the record and just very briefly summarize some of the points.

Senator GRASSLEY. Yes; your whole statement, and anybody else's statement, will be included in the record as submitted. We would encourage you to summarize. We do have the light that goes on. It is not an absolute prohibition to continue any further, but I would appreciate it, as soon as the light comes up, that you would wrap up as quickly as possible.

Mr. SCHUTZMAN. I expect to beat the light.

Senator GRASSLEY. OK. Proceed.

Mr. SCHUTZMAN. Thank you, Mr. Chairman.

Currently we are in the second year of operation, and with preparations made for the commencement of the third year of the tax refund offsets.

We believe, by any standard, the tax offset program has proved to be a major success. It is a joint effort by the Internal Revenue Service, my office, the Office of Child Support Enforcement, and State and local child support agencies.

Each of the participants in this enterprise fulfills a vital function, and the success witnessed to date is evidence of the quality of the work performed by all.

I would like to briefly describe the process used to offset tax refunds:

Once a year, before October 1, all States submit to my office for transmission to the IRS a list of individuals who are delinquent in fulfilling their court or administratively ordered support obligations to families who are AFDC recipients.

The submittal includes notification by the State's child support enforcement agency director that all cases meet the following requirements: Support obligation must have been established by a court or administrative hearing, the amount of obligation is delinquent for at least 3 months, and the amount owed is more than $150.

Beginning with the second year of operations, a pre-offset notice was sent to all individuals submitted for offset telling them that such action has been taken. The notice is issued in October.

When we receive the information from the States, my office edits that information, works with the States in correcting any errors, and compiles one master tape which we transmit to the IRS by December 15. Each time a match is made with the IRS file, the IRS does flag their file.

When an actual refund is offset, a notice is sent from the IRS to the taxpayer stating the reason for the offset. A report from the IRS is sent to us, and the collected funds are also sent to us, and we disburse that on a monthly basis to the States.

The transfers of funds occur approximately from April through December of each year.

Accompanying the collected funds is a listing of home addresses of the absent parents whose refunds were offset. The address information facilitates further collection efforts on the part of the States.

At this time I would like to talk about the results, and to avoid any confusion, the numbers that I'm going to recite are slightly different than the IRS numbers. That doesn't mean we are in disagreement. For example, the number of offsets mentioned by the IRS was something like 279,000 for the first year. Actually, there may be included in those offsets some duplicates. We may hit a taxpayer two or three times, because he may submit amended returns for prior years.

Let me give you my statistics. As I said, we are not in disagreement; we just count differently.

The first year results: 561,000 cases submitted, 273,000 cases offset by IRS, and approximately $169 million collected.

After the first year we made a number of improvements to the program. First, working with the IRS and ourselves we added additional automation to the process in order to speed it up.

We also made some regulatory changes which included the issuing of a pre-offset notice, which affords individuals opportunities to settle the debt prior to the tax refund or to correct any error that may be in the notice.

And we also added a statement in our regulations to have the States formally have a mechanism for making prompt refunds to taxpayers that were erroneously offset.

In addition, we have audited through this year about 22 States to see what results—how they were operating the program, and ask them to improve.

Second year results: 872,000 cases were submitted by 50 States, 323,000 cases have been offset through the end of August, and we have collected about $170 million.

Additional program changes we are making this year: Complete automation of handling of amended joint returns, options for States to submit test tapes to us ahead of time so that we won't have a problem in processing them, and we have also expanded the timeframe for the States to submit deletions and modifications on previously submitted cases.

This concludes my summary. I will be glad to answer any questions—and I notice I did beat the red light.

[Laughter.]

Senator GRASSLEY. You will probably be the only one who does. Let that be a challenge to others.

[The prepared statement of Hon. Fred Schutzman follows:]

DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

FOR RELEASE ONLY UPON DELIVERY

STATEMENT BY

Fred Schutzman
Deputy Director
Office of Child Support Enforcement

Before The

Subcommittee on Oversight of The Internal Revenue Service

Senate Committee on Finance

On

Federal Income Tax Refund Offset Program

September 16, 1983

Mr. Chairman and members of the committee, I am here today to discuss the Federal Income Tax Refund Offset Program on behalf of the Child Support Enforcement (CSE) program. The CSE program is a Federal-State effort to establish paternity of children who have been deserted or abandoned, and to insure that the absent parents of welfare recipients and other dependent children provide support payments to their children. The main goals of the program are to insure that children are supported financially by their parents, to enforce family responsibility, and to reduce the cost of welfare assistance to the taxpayer.

I appreciate this opportunity to appear before you today, to talk about the Federal Income Tax Refund Offset Program. Currently in its second year of operation, with preparations being made for the commencement of its third year of tax refund offsets, the Tax Refund Offset Program, by any standard, has proved to be a major success.

The basis for this innovative and effective method for recovering child support owed to the State and Federal governments is Public Law 97-35, which provides for the collection of delinquent child and spousal support. This is accomplished through an offset of the individual Federal income tax refunds of obligated absent parents against their delinquent child support arrears. Cases to be offset are submitted to the Office of Child Support Enforcement (OCSE) for routing to the Department of Treasury by State Child Support Enforcement Agencies. As you know the law restricts State Agencies to submitting those cases involving families which have executed an assignment under the Aid to Families with Dependent Children (AFDC) program.

The Tax Refund Offset Program is a combined effort by the Internal Revenue Service (IRS), and State and local child support enforcement agencies. Each of the participants in this enterprise fulfills a vital function and the success witnessed today is evidence of the quality of the work performed by all.

THE FEDERAL TAX REFUND OFFSET PROCESS

Interim final regulations which specify the requirements for case submittal were published by OCSE February 19, 1982 in the Federal Register (47 FR 7425) and final regulations were published January 20, 1983 in the Federal Register (48 FR 2534). Once a year before October 1, all States submit to the OCSE, for transmission to IRS, a list of individuals who are delinquent in fulfilling their court or administratively ordered support obligations to families who are AFDC recipients. The submittal includes notification to OCSE by the State's Child Support Enforcement Agency Director that all cases meet the following requirements: The support obligation must have been established by a court or administrative order and the delinquent amount owed must be more than $150 and at least three months old. The submitting State must have taken assignment under Section 402(a)(26) of the Social Security Act, and must have made reasonable efforts to collect the delinquent amount prior to submittal for offset.

OCSE consolidates all State submittals into one computer tape and forwards it to the IRS. Beginning with the second year of operation, the State or OCSE at the States request, sends a "pre-offset notice" to each submitted absent parent alerting him to the fact that his name has been submitted to the IRS for tax refund offset. IRS compares the OCSE submitted taxpayer information with its taxpayer master file, matching Social Security numbers with surnames. OCSE is then notified of any cases that do not match and in turn, notifies the States.

Each time a match is made, IRS flags its master file to freeze any potential refund that may become available. The IRS will, when possible, withhold (offset) the refund and issue a notice to the taxpayer. Listings of tax refunds that have been offset are sent to OCSE weekly and collected funds are deposited in a designated account for disbursement monthly to the States.

OCSE prepares the necessary detailed reports for the individual States and then arranges to transfer the tax refund collections to the State. These transfers are received each month, from approximately early April through December, along with a listing of the home addresses of the absent parents whose refunds were offset. This address information is valuable in itself in that it provides the local Child Support Agency location information whereby further collection efforts can be made. OCSE will bill the State for the processing of each collection. In its first year of operation, OCSE negotiated with IRS a cost per case of $17. The cost per offset for tax year 1982 is $11 due to improved procedures. We expect even further reduction in cost for the upcoming year.

FIRST YEAR RESULTS

As I mentioned earlier, the offset program has been extremely successful. In its first year of operation, forty-seven (47) States and the District of Columbia submitted over 561,000 cases for refund offset. The average arrearage amount on these cases submitted was $3,800. Ultimately offsets were made on 273,090 cases for a total net collection of $168,915,280. The average collection per case offset was $620. Cost of the Program as billed to the States was $4,542,247. (70% of which is reimbursed by the Federal government).

This $168 million amounted to 20% of the States' total AFDC collections in 1981. Nonetheless, even before the first year's collection reports were fully tabulated, IRS and OCSE set out to improve the procedures of the offset program in order to make a good program even better.

IMPROVEMENTS TO PROGRAMS OPERATIONS

The strategy taken by IRS and OCSE in terms of improvements to the offset program consisted of a twofold approach: the first goal was full automation of the process; the second was regulatory protections to ensure the efficient operation of the tax refund offset program while protecting the rights of the taxpayer obligors.

The automated systems component of the Program has been enhanced, increasing the efficiency. The full automation of the Program's procedures increases the efficiency of the offset process both in terms of quality of the collection reporting and the swiftness with which the reporting is now accomplished.

With respect to regulatory changes, a number of improvements have been made to the Program. The issuance of the pre-offset notice, either by the State or OCSE, has been adopted and serves to provide the taxpayer-absent parent the opportunity to consult with the submitting State Agency to resolve any dispute concerning the accuracy of the support arrearage. This addition to the Program is considered to be most valuable in the sense that early awareness on the part of the taxpayer/absent parent of the potential offset of his or her tax refund can prevent most erroneous offsets and in some cases encourages settlement of the child support owed without the need of a tax refund offset at all. In short, affording the absent parent the opportunity to resolve the case prior to IRS offset has proven beneficial not only to the Program's operation, but to also foster individual parental responsibility. Other regulatory enhancements include: requiring States to promptly refund any amounts erroneously offset and requiring States to verify accuracy of arrearages prior to certification for tax refund offset.

It is hoped that the changes made in the final regulations will alleviate most of the concerns of taxpayer/obligers who have challenged the offset process in Federal Court. These concerns have focused on two main issues: 1) Whether the taxpayer is entitled to formal notice and hearing prior to offset; and 2) whether joint returns may be intercepted in States where an absent parent's spouse is not liable for the child support debt.

Further, in an effort to assist the States in recognizing what problems that may exist with respect to the accuracy of submitted case files, OCSE conducted an audit during January through May of 1983. Twelve states were

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selected for review. The audit produced a heightened awareness of some of the weaknesses found in case submittal and served to correct these weaknesses.

SECOND YEAR RESULTS

The procedural modifications and systems enhancements implemented for the second year of offset processing appear to have fulfilled their intended purposes. For the 1983 processing year (tax year 1982) , fifty (50) States and three (3) jurisdictions submitted 872,328 cases for potential offset. This represents a 55% increase in number of cases submitted for offset, and an addition of three (3) states and three (3) jurisdictions to the Program. The average arrearage amount on these cases was $3500.

As of August 31, 1983 offsets were made on 323,129 cases for a total of $169,353,506. The average collection per case offset was $524. Thus, with additional processing still to occur, we find that we have already made offsets in 50,000 additional cases over last year. The cost to date rests at $3,550,525.

In response to concerns for joint taxpayers, changes have been made in the notice IRS issues to inform the non-obligated spouse concerning the right to claim his or her share of the tax refund. This is done, for up to 3 years after the year the tax liability was incurred by filing a 1040X amended return. Upon receipt of this notification (filing of a 1040X) from the non-obligated spouse, IRS will directly refund the non-obligated spouse's share of the amount offset and will adjust the State collection by the amount refunded.

During the first year, payments made by the IRS to the non-obligated spouse caused some problems for State Agencies, especially when the State had previously refunded the collection to the taxpayer because no past due support was owed. OCSE and IRS developed new procedures that were

designed to prevent the taxpayer-absent parent from receiving two payments on these cases, and the State from subsequently ending up in a deficit situation as a result of IRS making an adjustment.

For next year OCSE and IRS will be automating the current manual process for the verification of a State payment to taxpayers. The State will forward on a weekly basis, the amount of all refunds made to absent parents, so that these transactions can be marked on the IRS file and considered in the event that the taxpayer seeks a duplicate payment from IRS.

CHANGES FOR 1984 PROCESSING YEAR

Foremost amongst additions for the upcoming year was the option on the part of the States to submit a test tape of support cases for processing by OCSE. This test tape processing allowed the States to verify their own systems formats and case data before the final submittal deadline of October 1. Thus, errors detected as a result of the test tape processing, can be corrected before the final tape submittal resulting in a much more accurate and hence fruitful case file.

Also of significance is the extension of the time frame in which deletions of cases previously submitted can be made. In the upcoming year, deletions can be made up to April 30. This extended time period allows for modifications to be made as a result of either the State recognizing a mistaken submittal or the absent parent paying his support obligation so as to avoid tax refund offset.

For your information, nearly every State which has a State income tax has legislation providing for, or has already implemented a comparable procedure to the Federal Income Tax Refund Offset Program. State income tax refund intercept and other debt setoff processes have gained widespread acceptance and been quite successful in collecting delinquent child support, student loans, and other obligations owed to State governments. Several States have even extended this process to families not receiving AFDC under the CSE program.

In short, I would like to say that as we approach the beginning of the third year of the tax refund offset program, we do so with a great deal of satisfaction and pride over our past accomplishments, yet fully expect to surpass those levels for processing year 1984.

Thank you again for this opportunity.

Senator GRASSLEY. I want to ask some questions.

Oh, do you have a statement, too?

Ms. GOEDDES. No, Senator, I don't.

Senator GRASSLEY. Oh, I thought you were getting ready to speak, and I didn't want to ignore you if you did have a statement.

I want to ask questions similar to what I asked of the first two witnesses, not necessarily to find out if there is any difference or to verify one against the other but to get your point of view. Again, I would refer to the 1975 act in which Congress gave the IRS the authority to collect delinquent child support enforcement accounts as they would collect delinquent taxes, and they said they had about 150 cases submitted to them. Would you agree to that?

Mr. SCHUTZMAN. I think he was talking about last year.

Senator GRASSLEY. Oh, last year.

Mr. SCHUTZMAN. Since 1975 through the end of fiscal year 1982, 1,364 cases have been submitted to the IRS, amounting to $9.3 million. Of that $9.3 million, $1.3 million has been collected.

In fiscal year 1982, for example, to help the Commissioner in his testimony, there were 160 cases submitted and about $564,000 collected.

In the first half of this year, only 73 cases have been certified.

There are a number of problems with that process, and we think also that the current IRS tax offset has also a simpler, cheaper method for collecting arrearages. We think that the States are going to use this process even less, even though it has been a meager use; although some States do use it extensively, but it is only a handful—two or three, really.

I think the reluctance relates to cost, complexity, and the length of the process. The complexity comes from the documentation required for the State to submit to the IRS for full collection. For example, they need identification of the case, they need a copy of the court order, and any arrearages related to that court order: they have to document what attempts they have made to collect, why the attempts have failed, and they have to try to identify the assets. This is a complex process, and it has not been used extensively.

Senator GRASSLEY. Would you generally say that the child support refund offset program has been effective in reducing welfare costs? Or are we still not doing the things to make it really effective?

Mr. SCHUTZMAN. No; we think it is an extremely effective program. If one looks at the total collections for the 2 years, we are estimating in excess of $340 million, and those are direct welfare costs. So it has been extremely effective in reducing the welfare costs.

Senator GRASSLEY. Are there any particular problems with the current offset program that need to be corrected?

Mr. SCHUTZMAN. As I indicated earlier, we have been working closely with the IRS and with the State and local folks, because we did come across some process kinds of problems. We have made a number of improvements in the process, and we think the IRS will fully automate, we will be fully automated next year, and the process will go very smoothly we believe.

Senator GRASSLEY. What does it cost your Department, HHS, to create a tape listing all of the certified delinquent payors which are submitted to you by the various States?

Mr. SCHUTZMAN. Creating a tape is very simple, but one has to talk about just more than creating a tape but the process that we go through—the edit, the correction, the back and forth with the States. I would say that we use about seven or eight people in this process all during the year, both our computer-type people and the people that deal with the States on problems.

Senator GRASSLEY. Do you classify that, then, as relatively inexpensive?

Mr. SCHUTZMAN. Relatively inexpensive.

Senator GRASSLEY. And very cost-effective?

Mr. SCHUTZMAN. Yes.

Senator GRASSLEY. Has there ever been an attempt to find out what the States put into all of this? I don't suppose that is possible.

Mr. SCHUTZMAN. We have been talking to the States. And you know, as the Commissioner of the IRS indicated, the States would charge $17 the first year of operation, $11 this year, and probably less next year; but in addition to that, they have to put their list together to make sure that the arrearages are correct. They will be appearing before you today. I suggest you do ask them that question. We do not have that data.

Senator GRASSLEY. OK.

Is the Department of HHS employing any other methods to collect delinquent child support payments?

Mr. SCHUTZMAN. As you know, the program is administered by the State and local folks and not by the Department of HHS, but I could talk about some other enforcement techniques that have been used.

We are allowed, for example, to offset unemployment compensation for past-due child support. This past year we are estimating we will have collected approximately $15 million through that process.

As you know also, in our administration's bill we have talked about some other enforcement techniques such as mandatory wage assignment, State income tax offset. We feel those are the most cost-effective, simple methods for increasing child support enforcement.

In addition, of course, in order to speed the process, we also have in our bill the provisions for a quasi-judicial or administrative hearing to speed the process through the court system, through the legal process.

Senator GRASSLEY. OK.

Mr. Schutzman, could I ask you, just stay there, but to halt answering my questions. Senator Percy came in, and if you are ready, Senator Percy, we would break in right here, into my questioning of Mr. Schutzman, for your testimony.

Senator PERCY. Well, I very much appreciate that, Mr. Chairman.

Senator GRASSLEY. Mr. Schutzman is with the Department of HHS. Would you proceed?

A Senator from Illinois, who is chairman of the Foreign Relations Committee and on television every night, doesn't need any sort of introduction.

STATEMENT OF HON. CHARLES PERCY, U.S. SENATOR FROM THE STATE OF ILLINOIS

Senator PERCY. I bring with me my credentials as Chairman of the Foreign Relations Committee by having with me one of the most distinguished diplomats in one of the most troubled parts of the world. We were in the midst of our conversation and had not completed it, so I just asked him to come right along, the Prime Minister of Cambodia, Prime Minister Son San, who is a man much admired around the world, who is fighting a bitter fight for the freedom of his own country. And we, of course, along with many of our allies, have been anxious to help him. So we warmly welcome him to the Senate, but I know you would want to warmly welcome him, also, to the Senate Finance Committee.

Senator GRASSLEY. We welcome you, Mr. Prime Minister.

Senator PERCY. Mr. Chairman, the subject that you are dealing with is a subject that has been close to my heart for a long time. I have frequently commented to the Government Affairs Committee that if we ran any private corporation the way we run the Federal Government we would be totally bankrupt. There is no way any organization other than a government could operate the way we do, and it's about time we really changed some of those methods.

When we consider that we are the largest lending agency in the world—we have about 130-some agencies of the Federal Government that loan money—we are not only efficient in loaning it out, we are inefficient in collecting it. With $147 billion outstanding in loans, almost $40 billion is in default. Now, that's just a totally unacceptable record.

As I analyzed and appraised why, I found that it was just as much the fault of the Government as anything else, in fact more so—very poor methods that are used. The very fact that, for instance, I don't know of a bank in this country that would loan money without getting a social security number. The Federal Government is prohibited from asking for that social security number.

We don't hire outside collection agencies when we can't get it ourselves. We can't report to a credit bureau a bad debt. We weren't even notifying the other 129-130 Government agencies when there was a default with one agency. We found people who would go down a list of eight agencies or so and default one after the other, the one agency not knowing the other had defaulted.

So we now are focusing on a particular aspect of it that I think is a proven and useful tool. And I do want to thank you very much indeed for giving me this opportunity to testify.

This hearing is the first time the Finance Committee has looked seriously at the proposal to offset tax refunds as a means of collecting defaulted student loans since the idea was first proposed in 1979.

I compliment you for your leadership in bringing this issue before the committee today.

I will take just a few minutes to describe the Government's debt-collection problems, the legislation passed last year to deal with it, and why I feel strongly that a carefully implemented tax refund offset program could be and should be undertaken.

Over the past 3½ years I have held eight hearings on the debt collection issue in the Government Affairs Committee. The Government's debt collection story is, as I have said, one of the most shocking examples of Government waste that I have seen—Government waste, fraud, and mismanagement.

Every time I hold another hearing, another horror story of waste gets—the whole story gets more unbelievable. For example, we found in testimony that was given, and I called various universities up to see why they weren't collecting student loans. I found a reluctance on the part of Harvard to call. I finally had to call up the President of Harvard and say, 'Look, we want your people up here, and we're going to see that they do come. And we would like them voluntarily.' But the record was so bad. Here is one of the great business schools in the country, and for a great university one of the worst collection records.

We found that one out of four Harvard doctors who received student loans were in default. Well, those doctors were earning over $200,000 a year; they had an unblemished credit record. They belong to country clubs, they own good-sized foreign cars—a perfect record, except they had never paid their student loan back.

And it is probably not the doctors' fault. The word gets around campus, You just don't have to pay. These are gifts, probably. Just get lost.

Answers to the letters come back, Addressee unknown. Three of them come back, and you are probably dropped off the computer.

So we had to strengthen our business procedures, and we have done that through the legislation that was enacted last year. We have already seen absolutely dramatic results.

I went over to the Department of Education, because I was horrified to find that, of the Federal Government, a total of 46,000 Federal employees who are receiving paychecks every twice a month had defaulted on their student loans. Five hundred of them had Ph. D.s and masters degrees in the Department of Education, making up to $50,000 a year. And I went over to officially notify them, with Secretary Bell, that we were going to garnishee wages, because the Government has never been allowed to garnishee wages before.

The legislation we passed last year that I had introduced, that we overwhelmingly supported—and I believe you were a cosponsor of it, Senator Grassley——

Senator GRASSLEY. Yes.

Senator PERCY [continuing.] Now gives us the power to do so. And we were going to use that power in the Department of Education.

I think for the most part we found we didn't have to use it. As soon as they knew we really meant business, that that was a loan not a gift, they were expected to pay it back and they were going to bet a 25-percent garnishee from their wages, they started to pay.

So, it's a matter of responsibility of the Government to bring its procedures in line, procesures I think we find in the private sector.

The dramatic illustrations that we have had show that the $40 billion of money owed us that is in default now, which is equivalent to $400 for every taxpayer in the United States, is a collectible debt.

For this year we have forecasted about a billion dollars collected of brand new money through just the implementation of this law. We have already collected $2 billion. Next year we estimated $3.5 million; now, the minimum estimate will be $4 billion for next year. So we are making progress. But the step we are now suggesting be taken will be even a more dramatic illustration of what can be done.

Senator GRASSLEY. Is that $4 billion just education loans?

Senator PERCY. No; this is overall. Yes, because the student loans totaled $6.5 billion, of which $3 billion is in default, about half of it, which is a terrible record.

Mr. Chairman, no less than 17 States are now offsetting tax refunds as a means of collecting other debts, and they have had tremendous success with this method. Here, the Federal system helps a great deal. You can test out and try it out on a number of States before you go national.

Oregon, for instance, is collecting $15 for every dollar it spends on the program. There is absolutely no other way of collecting defaulted government loans that will return $15 for ever dollar spent on collecting.

A preliminary study of potential savings in such a program conservatively estimated that $400 to $600 million could be collected in 2 years, money that otherwise would be written off.

I have brought with me a draft bill I intend to introduce which would establish a tax refund offset program for collecting defaulted Government loans. Unlike Senator Jepsen's bill, my proposal would not treat unpaid student loans or other Government debts as taxes due. Rather, it would simply allow income tax refunds to be offset. The bill implements an offset program on a limited basis. I believe that my proposal addresses many of the IRS's concerns. Here is how it would work:

First, the tax refund offset program would be authorized as a 1-year test, to determine the effectiveness of the program and test whether the program had any adverse effects on the IRS or tax system. At the end of 1 year, the program could be continued or expanded if the Congress so desired.

Second, only those debts that had court judgments established in their validity would be subject to refund offsets during this pilot project. There are at least 65,000 claims, worth $1 billion, at the Justice Department which have not been collected. Many of these claims have judgments. Using judgment cases would assure that due process has been provided the debtor.

Third, the offset could be used for collecting all types of defaulted Government loans, not only student loans. Student loans represent only about 10 percent of the defaulted debt; thus, there is no reason to exclude the rest.

I would also propose that unpaid criminal fines be subject to refund offset. That's one of the last phenomenons we have run into. With the jails crowded, jammed, more and more judges are fining people. But here again, it proves crime does pay. It's like

going down, take him down to the prison, and say, "Oh, the prison's filled. We can't put you in there. You are fined." And then we don't make any effort to collect that fine. Even Gordon Liddy, after all, was fined $40,000. And until the pressure was put on him and it was realized how much money he had made writing books and making lectures, that he was forced to pay that $40,000. He just hadn't paid it.

We are down now to the point where defaults are about two-thirds of the total amount in recent years. It's getting worse, steadily worse, not better. So certainly an offset for criminal fines—there should be no question about it. Should the Government pay back an overpayment on a tax, for instance, to someone that is owing the Government money on some other account? What is the matter that we can't, with computers, pull this together and not pay the person who is owing a criminal fine to the U.S. Government?

In hearings I held in July it was discovered that criminal fine collections have dropped off dramatically, and collecting them drains precious resources from the U.S. attorney's office. There are over $100 million in uncollected criminal fines right today.

Over the past few years, opponents of tax refund offsets have made several arguments against the program. Frankly, I don't believe that many of these arguments hold up when examined carefully. Let's look at a couple of them just head-on:

There is no evidence that an income tax refund program would threaten voluntary compliance by taxpayers. In fact, the evidence seems to show the opposite; 17 States have been using these programs that would threaten voluntary compliance by taxpayers, and there has been no real evidence of that at all.

Absolutely not a single State have we found where there is a drop in the voluntary compliance. At the Federal level there is no reason to believe that child support offsets have had adverse effects; moreover, if the program were implemented as I proposed, a 1-year test, we could monitor any adverse effects. It seems to me that a vast majority of taxpayers would be grateful to see the Government taking action to recover defaulted debts.

Those subject to offset would be assured their due process rights, because only judgment cases, as I've said, would be offset.

An offset program at IRS would not divert resources away from their primary mission and make the IRS the Government's debt collector.

I propose that the defaulted loans not be considered taxable income; thereby, not requiring IRS to go through its lengthy procedures for tax collection. Rather, IRS would simply match two lists of social security numbers by computer, send out one notice to each debtor to be offset, then reduce the refund amount accordingly.

Again, in the test program only a small sample of cases would be offset. I would support, and I believe the administration would support, based on discussions that I have had with OMB, giving the IRS the additional resources needed to do this task.

Joint tax returns do represent a problem to an offset program, but not an insurmountable one. In Oregon, those who filed joint returns but may have incurred their debts as individuals are notified before the offset, to give them the opportunity to contest a portion

of the offset. It may be necessary to offset only individual returns in the pilot project.

In summation, I feel it important, Mr. Chairman, to remember that in general when Uncle Sam loans money to students, small business people, and others, it is the lender of last resort. The Government is often taking the risk that no bank would take. There is often no collateral, the debtor has no established credit, and may not even be employed. When one of these individuals defaults and all of the routine collection measures have been taken, including a judgment in Federal court, it seems to me that the Government has every right to offset a tax refund that would be given to the person otherwise. I urge the committee to report legislation along the lines that I have proposed.

I thank my colleagues here at the table for their very great thoughtfulness in yielding to me.

Senator GRASSLEY. I will simply thank you. I have no questions, but I am glad that you alluded to the fine piece of legislation that you steered through the Congress last time and your testimony also included statements of how it has accomplished its objectives.

I want to congratulate you on your past success, and I am glad see you haven't given up yet.

Senator PERCY. Thank you very much, indeed, Mr. Chairman.

[The prepared statement of Senator Charles H. Percy follows:]

STATEMENT OF SENATOR CHARLES H. PERCY

Mr. Chairman, I would like to thank you for giving me this opportunity to testify this morning. This hearing is the first time the Finance Committee has looked seriously at the proposal to offset tax refunds as a means of collecting defaulted government loans, since the idea was first proposed in 1979. I compliment you for your leadership in bringing this issue before the Committee today. I would like to take a few minutes to describe the government's debt collection problems, the legislation passed last year to deal with them, and why I feel strongly that a carefully implemented tax refund offset program could be, and should be, undertaken.

Over the past three and a half years I have held eight hearings on the debt collection issue in the Governmental Affairs Committee. The government's debt collection story is, I believe, the most shocking example of government waste, fraud, and mismanagement that I have encountered in my 17 years in the U.S. Senate. Each time I hold another hearing, the horror stories of waste get more unbelievable. For example, we found out that one out of four Harvard doctors who received student loans were in default. We discovered that the government's own employees were defaulting on their student loans -- 46,000 in all. These dramatic illustrations are, unfortunately, only the tip of the iceberg in terms of the scope of this problem. Government-wide, unpaid delinquent debts now exceed $40 billion -- or more than $400 for each taxpayer in this country.

This disastrous situation is now starting to turn around. With the committment of the Reagan Administration, and with new legislation enacted last year, over $4 billion more will be collected in fiscal year 1984. Four billion dollars more. But much more could be collected, especially from those who owe less than $1000, if the government were able to use tax refund offset as a last resort.

Mr. Chairman, no less than 17 state governments are offsetting tax refunds as a means of collecting other debts -- they have had tremendous success with this method. Oregon, for instance, is collecting $15 for each dollar it spends on the

program. There is absolutely no other way of collecting defaulted government loans that will return $15 dollars to every dollar spent on collecting. A preliminary study of potential savings from such a program conservatively estimated that $400 to $600 million could be collected in two years, money that would be written off otherwise.

I have brought with me, a draft bill I intend to introduce, which would establish a tax refund offset program for collecting defaulted government loans. Unlike Senator Jepsen's bill, my proposal would not treat unpaid student loans, or other government debts, as taxes due. Rather, it would simply allow income tax refunds to be offset. The bill implements an offset program on a limited basis -- I believe that my proposal addresses many of the IRS's concerns. Here is how it would work:

- The tax refund offset program would be authorized as a one-year test, to determine the effectiveness of the program and test whether the program had any adverse affects on the IRS or tax system. At the end of one-year, the program could be continued or expanded, if the Congress so desired.
- Only those debts which had court judgments establishing their validity would be subject to refund offsets during this pilot project. There are at least 65,000 claims, worth $1 billion, at the Justice Department which have not been collected. Many of these claims have judgments. Using judgment cases would assure that due process had been provided the debtor.
- The offset could be used for collecting all types of defaulted government loans, not only student loans. Student loans represent only about 10 percent of the defaulted debt, thus, there is no reason to exclude the rest. I would also propose that unpaid criminal fines be subject to refund offset. In hearings I held in July, it was discovered that criminal fine collections have dropped off dramatically and collecting them drains precious resources from the U.S. Attorney's offices -- there are over $100 million in uncollected criminal fines.

Over the past few years, opponents of tax refund offset have made several arguments against the program. Frankly, I don't believe that many of their arguments hold up when examined carefully. Let me address them head on:

- There is no evidence that an income tax refund program would threaten voluntary compliance by taxpayers. In fact, the evidence seems to show the opposite. Seventeen staes have been offsetting state income tax refunds and none have reported a drop in voluntary compliance or an increase in adjusting withholding to avoid refund confiscation as a result of their offset programs. None. At the federal level, there is no reason to believe that child support offsets have had these adverse effects. Moreover, if the program were implemented as I propose -- a one-year test — we could monitor any adverse affects. It seems to me that the vast majority of taxpayers would be grateful to see the government taking action to recover defaulted debts.

- Those subject to offset would be assured their due process rights because only judgment cases would be offset, they have already had their day in court.

- An offset program at the IRS would not divert resources away from their primary mission and make the IRS the government's debt collector. I propose that the defaulted loans not be considered taxable income, thereby not requiring IRS to go through its lengthy procedures for tax collection. Rather, the IRS would simply match two lists of social security numbers by computer, send out one notice to each debtor to be offset, then reduce the refund amount accordingly. Again, in the test program, only a small sample of cases would be offset. I would support, and I believe the administration would support (based on discussions I've had with OMB), giving the IRS the additional resources needed to do this test.

- Joint tax returns do present a problem to an offset program, but not an insurmountable one. In Oregon, those who file joint returns, but may have incurred their debt as individuals, are notified before the offset to give them an opportunity to contest a portion of the offset. It may

be necessary to offset only individual returns in the pilot project.

I feel it is important to remember that, in general, when Uncle Sam loans money to students, small businessmen and women, and others, it is the lender of last resort. The government is often taking a risk that no bank would take — there is often no collateral, the debtor has no established credit, and may not even be employed. When one of these individuals defaults, and all other routine collection measures have been taken — including a judgment in federal court — it seems to me that the government has every right to offset a tax refund.

I urge the committee to report legislation along the lines of what I have proposed.

Senator GRASSLEY. I think the IRS referred to this, but I didn't ask them for clarification, and I would like to know what the average amount of child support recovery is when we use the offset method.

Mr. SCHUTZMAN. In the first year the average offset that we recovered was $624. This year it is running about a hundred dollars less, about $525.

Senator GRASSLEY. Can you explain that downward trend?

Mr. SCHUTZMAN. I think it is probably related to the economy.

Senator GRASSLEY. Is there any way we could estimate the size of debt owed back child support from non-AFDC families?

Mr. SCHUTZMAN. There has been some data from the 1981 census report which was issued just this year. I would say that there were 6.4 million families, non-AFDC families, 3.4 of those were due child support, and 2.6 million received full child support; 1.2 million received nothing, and we estimate from that report that there was about $2 billion in 1981 owed in child support for non-AFDC families, for those who have court orders.

Senator GRASSLEY. My next question, then, would be: Of that $2 billion that is uncollected and owed, how much do you think we could get from the income offset if it were extended to non-AFDC families?

Mr. SCHUTZMAN. Again, one would have to look at the specifications. For example, there are some bills before the Congress today that say all the people should be involved—all children should be involved—in the child support collection enforcement efforts. Other people say that it should be only those folks who apply for the services; why should we interfere with private problems and debts owed between two private persons?

So, depending on how one specifies the number of people that would enter the system, and it would probably be slow—we have attempted to make some estimates, but it depends on the specifications. As I said, there is approximately $2 billion owed from 1981. Some portion of that would be collected, and it would have to be a guess. We could make some assumptions and make those guesses.

Senator GRASSLEY. So in other words you are saying it is practically impossible to be very——

Mr. SCHUTZMAN. Well, to be precise. But one could make some assumptions and say that, compared to the current program, one can collect x number of dollars.

Senator GRASSLEY. Well, then, let's just assume that we make the program available to non-AFDC families, and let them apply for it. You would have to assume a certain percentage would apply; that would be a certain percentage of the $2 billion owed. Have you done it that way?

Mr. SCHUTZMAN. As I have indicated, you know, it depends on which assumptions you want to make.

Senator GRASSLEY. I guess I am just asking you to report on whatever assumptions you have made.

Mr. SCHUTZMAN. We have not finalized our estimates because we are waiting for some specifications.

Senator GRASSLEY. Well then, the proper thing for me to do would be to ask you to submit that to us when you get that.

Mr. SCHUTZMAN. Sure.

Senator GRASSLEY. How much would the extension of the program to non-AFDC families increase the costs for your Department?

Mr. SCHUTZMAN. Again, as you know, we fund 70 percent of the State and local costs, and that's where most of the costs would occur. And, again, it depends on how one sets up the process.

For example, it may be required, in order to establish what the arrearages are—there may be disagreement between the two parties—it may require a court hearing, and therefore that could be very expensive. You may have to reduce the amount of the judgment or go to court first, before you can actually submit the amount. In other words, determining the arrearages is extremely difficult.

So, again, it depends on how the process is specified and how each State could work it out. And some States do have data—very few—on what the arrearages are in non-AFDC cases. Most States do not.

Senator GRASSLEY. OK.

I'm sorry we can't answer that question. Maybe I am expecting too much. Maybe what I ought to do is just ask you to think about it.

Mr. SCHUTZMAN. Well, we have been. And we have talked to some of the State folks, and they will be up here testifying. It will be much more costly than the AFDC, because, again, that's where we do have the data available because it is related to welfare payments. It is very difficult to determine the number. It would be a complex process.

Senator GRASSLEY. I will go on, then, to another point.

I don't know to what extent you can divide up delinquent parents into low, middle, and high income individuals, but my question comes from the proposition of whether high income individuals might be more sophisticated in avoiding the offset by claiming additional exemptions to reduce their refunds. Is there any evidence to that effect?

Mr. SCHUTZMAN. Again, I think that would probably be produced in part by the study that the Commissioner of IRS talked about earlier today.

Senator GRASSLEY. You have no evidence now?

Mr. SCHUTZMAN. We have no evidence concerning that.

Senator GRASSLEY. OK. Do your records include just the division of people in the income categories, so that we know whether low income or high income people have a better record of fulfilling their responsibilities?

Mr. SCHUTZMAN. We do not have specific data on that. However, there was a Stanford University study in 1962, and it is related to California. It shows that there is little relationship between income and noncompliance. In other words, men with incomes between $30,000 and $50,000 a year were likely to fail to comply as those with incomes under $10,000. So it is equally spread across the spectrum.

Senator GRASSLEY. OK.

Do you have any idea as to what percentage of AFDC child-support accounts were collected by States before the Federal Government started to assist through these two programs?

Mr. SCHUTZMAN. The only evidence we have is, in 1975 there was a study done by the then Department of Health, Education, and Welfare. It showed that for AFDC families they collected $126 million.

After the Federal legislation was passed, in 1976 we collected $200 million on behalf of AFDC families, and in 1982 we collected almost $800 million, which will give you some sort of order of magnitude.

Senator GRASSLEY. What is the percentage for today?

Mr. SCHUTZMAN. I have some percentages. We collected, free child support Federal involvement, the current 4-D program as we call it, in 1975 we collected about $126 million in child support on behalf of AFDC families. Today we are collecting about $800 million.

The percentages of cases we collect from have varied between 10 and 11 percent over the short life of this program. We collect about 10 or 11 percent of the cases.

Senator GRASSLEY. That's my last question. I want to compliment you on your testimony and your answers to my questions, and I will look forward to that additional information that I requested to be submitted.

Mr. SCHUTZMAN. Thank you very much.

Senator GRASSLEY. Thank you very much.

[The information follows:]

Question. What are your estimates for the collections that could be achieved under a non-AFDC Federal income tax offset process: What would it cost?

Answer. Based on the latest consus data regarding female headed households and on IV-D experience, we believe 800,000 non-AFDC cases would be prepared and submitted for the 1984 tax year, incurring administrative costs during fiscal year 1984. However, these expenditures would not produce an increase in child support collections until fiscal year 1985. As the population becomes aware of this service, the IV-D caseload is expected to grow quickly, generating 1.2 million non-AFDC cases for IRS offset in fiscal year 1986 and 1.5 million thereafter. Each year, starting in fiscal year 1984, approximately 500,000 cases will require a hearing, either administrative or court, before the arrearage can be determined accurately. The range of costs presented below reflects the cost variations associated with the type of hearing, as well as IV-D administrative costs. We have assumed a 45 percent collection rate (fiscal year 1982 actual), current law FFP of 70 percent, and a $525 average IRS offset (fiscal year 1983 actual) using the latest available data relating to the offset for AFDC cases.

The Federal and State governments do not retain any part of the non-AFDC collections. Non-AFDC collections are paid to the family. These estimates do not include welfare cost avoidance savings which are the funds saved by the Federal and State governments when a family is removed from or remains off the welfare rolls because of the receipt of child support.

[Dollars in millions]

	Fiscal years			
	1984	1985	1986	1987-89
Collections	0	$190	$280	$350
Costs	$93-250	115-270	130-285	130-285
Federal	65-175	80-190	90-200	90-200
State	28-75	35-80	40-85	40-85

Senator GRASSLEY. Our next witness is testifying for the Department of Education, Dr. Edward Elmendorf, and he has been Assistant Secretary for Postsecondary Education since December 1982. He happens to be the administration's principal spokesman for higher education policy. He has also served as Deputy Assistant Secretary for Student Financial Assistance, in charge of student loan programs, and I understand you hold a degree in higher education administration from the University of Massachusetts?

Dr. ELMENDORF. Yes, sir.

Senator GRASSLEY. And would you introduce your associates?

Dr. ELMENDORF. This is Mr. Jack Reynolds, Mr. Chairman, who is in the Department of Education, working in the Office of Student Financial Aid as head of our debt collections task force.

Senator GRASSLEY. OK.

Would you proceed as I have instructed previous people to so do?

Dr. ELMENDORF. Yes, sir. I would hope that you could accept our statement for the record, and I will try to summarize it in about 10 minutes.

Senator GRASSLEY. OK.

[The prepared statement of Hon. Edward M. Elmendorf follows:]

Statement by Edward M. Elmendorf

Assistant Secretary for Postsecondary Education

U.S. Department of Education

Before the Senate Subcommittee on Oversight of the Internal Revenue Service

Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to be here today to discuss the Department's loan collection activities in the student financial assistance loan programs and to comment on S. 150, the "Collection of Student Loans in Default Act of 1983."

In the past two years, the Department's student loan collection effort has been significantly strengthened through legislative initiatives introduced in the 96th and 97th Congresses. These new authorities have provided us with tools which are necessary to successfully address such an important recovery effort. We are proud of the progress we have made in improving our collection efforts on defaulted student loans. Among the major initiatives that we have successfully implemented within the past year are:

-- full implementation of private sector collection agency contracts;
-- more timely use of Internal Revenue Address Locator Services;
-- a pilot project with the Internal Revenue Service to determine the feasibility of taxing as unearned income student loans which are written off;
-- improvements in collection system software which have enabled us to more effectively address the new authorities provided by the Debt Collection Act of 1982;
-- development of the procedures to implement the identification, location, and salary offset measures to collect from Federal employees in default on student loans; and,
-- implementation of administrative procedures which enable us to report

defaulted FISL and NDSL assigned borrowers to consumer credit bureaus.

These improvements have contributed to an increase in collections from a level of $46 million in FY'81, $55.5 million in FY'82, and current collections at a rate which is expected to result in excess of $70 million for FY'83.

These all-time high collection figures have been a direct result of the combined Federal-private agency collection activity. Our private collection contractors received their first assigned loans for collection in January of 1982. This cooperative collection activity produced $7.4 million in collections in the month of March, 1983 alone, which exceeded by $1.5 million the highest previous monthly total.

Even in light of these accomplishments, we believe that more can be done by the Department to build on them. In the near future, we will be transmitting a legislative proposal, "The Student Loan Collection Improvement Amendments of 1983", to further improve debt collection activities and default recoveries in the student loan programs. Included in that legislation are proposals which would:

- modify the procedure for disbursing funds under the GSL program. Under our proposal, loan checks payable to the student and the institution as co-payees, would be sent to the institution the student attends. We believe such a policy would provide better assurance that loans are used for educational purposes, and would reduce the potential for aid duplication, and the risk of "no show" defaults.
- expand and modify our current requirements for exchanging information on student defaulters with credit bureaus to provide that State

guarantee agencies, as well as the Secretary, be required to exchange such information. This would reduce new defaults while improving collections on existing defaults.

— broaden the student eligibility requirements to provide that a student may not receive financial aid if the student owes a refund on a grant or is in default on a loan made under title IV at any institution. Currently, the law provides only that a student in default or owing a refund may not receive further aid at the same institution.

— provide that the six-year Federal statute of limitations for filing suit for collection of a loan would apply to guarantee agencies filing such suit. If the applicable State limit is longer, the State law would still apply. Since these loans are Federally reinsured and subsidized, the Federal statute of limitations on recovery actions should be the minimum.

In addition to these Departmental proposals, the Department of Justice recently submitted legislation to the Congress authorizing the Attorney General to contract with private attorneys for the litigation involving Federal debts including student loan accounts. We believe that the threat of prompt litigation in those instances where such action is warranted will have positive effects. In the short term, the United States will be able to secure and enforce judgements in those cases where people have the ability to pay but have simply refused to honor their obligations. In the long term, the deterrent value of prompt litigation will stand as a reminder to those who are tempted to ignore their debts.

Your letter of invitation requested the Department's views on S.150, a bill which provides for the collection of delinquent student loans through income tax refund offsets.

The goal of the bill of providing the Federal Government with important credit management tools which will help to increase efforts to collect on student loans in default is laudable. We believe, however, that the actions we are undertaking are appropriate and sufficient at this time. With respect to S. 150's impact on the Internal Revenue Service and the Administration's position on this bill, we defer to the Treasury Department.

Mr. Chairman, I hope this testimony has been responsive to the concerns of your Subcommittee. I will be pleased to respond to any questions the Subcommittee members may have.

STATEMENT BY HON. EDWARD ELMENDORF, PH.D., ASSISTANT SECRETARY FOR POSTSECONDARY EDUCATION, DEPARTMENT OF EDUCATION, WASHINGTON, D.C.

Dr. ELMENDORF. I appreciate the opportunity to be here, and thank you for bringing to our attention your bill, S. 150, on which we will provide testimony, and also a chance to provide the subcommittee with an overview of the activities within the Department of Education that I think, unlike the subcommittee on Postsecondary Education, we have not had a chance to review with you. So if you don't mind us tooting our own horn, we would like to give you a little background on the seriousness of the problem, the magnitude of it, and some of the efforts underway to try to improve debt collection in the Department of Education.

Senator Percy was very accurate in stating that the amount of the total burden or debt to the Government as a result of defaulted student loans represents about 10 percent. To be more specific, it's about $3 billion that's owed the Department in the way of defaulted student loans. It breaks down into about $2 billion for the guaranteed student loan program, which is administered primarily by the States or the State agencies, and another billion dollars that is administered under the national direct student loan program by the institutions themselves.

Senator Percy mentioned Harvard. He was not talking about programs that are administered by the Department of Education; he was talking about a program administered by the Department of Health and Human Services.

We have about 2.4 million defaulted borrowers. About 1,300,000 of those borrowed State agency guaranteed loans, under the guaranteed student loan program, and about 1,100,000 borrowed directly from an institution under what we call the national direct student loan program.

What has caused the problem of defaulting on student loans? I think, first, years of inattention. Second, the lack of any appropriate debt collection tools which are available to the private sector but not to us, on which we might rely for collection; and kind of a pervasive attitude that it's OK for the Government to be generous in lending money but lenient in collecting its debts.

The President, in 1981, directed all Federal agencies to improve their information management, financial management, debt management, and funds disbursement systems. OMB issued bulletin 83-11, which required the agencies to set up credit management and debt collection task force efforts. The Department of Education has done that. A major part of our effort, in addition to collection, has been trying to set up a system that would avoid defaults in the first place. And that would be accomplished under what we call the Financial Aid Delivery System.

The Department's efforts have been significantly strengthened, as the Senator mentioned, through efforts by the 96th and the 97th Congress.

In the past year, we have implemented a number of major initiatives that were contained in the Debt Collection Act of 1982. As I just mentioned, under the Debt Collection Act we, for the first time as a Federal Government, got collection tools which the private sector had been using for a number of years.

There are three major initiatives I would like to talk about just briefly, the first of which is one of those tools we didn't have until the Debt Collection Act of 1982—and we do appreciate the effort by you and the rest of Congress for giving us that action.

We had not been able to, until now, refer delinquent student borrowers to credit bureaus. To me, that's one of the most popular ways of getting the attention of a defaulted student borrower, when their credit has been restricted or limited in other areas, areas that they now consider to be a higher priority than paying back their student loan.

We do have that authority. We have already negotiated with one agency; and we are negotiating with five other credit bureaus. We expect, within 6 months of final agreement, to have referred approximately 500,000 accounts to credit bureaus.

Second, as the Senator mentioned, we now have the ability to offset against Federal employees the amount that they are in default on their student loans.

As you probably have heard, we have identified 46,800 Federal employees who are in default on some $67 million in student loans. We have collected about $3.4 million of that as of August 14 on approximately 5,600 accounts.

The Senator did have somewhat of an inflated idea of the number of defaulters in the Department of Education. I think he put an additional zero on there. We identified, of the 46,860 Federal employees, 68 in the Department of Education. I am happy to report to you that every one of those 68 people have either paid or are in repayment on their student loans. We hope that the other agencies will be as aggressive.

I would like to also state that we have just issued regulations which allow other agencies to use the salary offset provision mentioned by the Senator. We can now offset 15 percent of the pay of any Federal employee who is recognized as in default on their student loan.

Third, unlike many other agencies, the Department of Education has gone forward with a major collection contract with the private sector. We have implemented, as of 1981, two major private sector contracts. Those two contractors started receiving their first loans

in January of 1982. Since that time we have transferred over 400,000 accounts to the two contractors, with the value of those accounts in the neighborhood of $640 million.

The actual improvements in collections have been very significant in the Department of Education. In 1981, we collected about $46 million. That jumped dramatically to $55.5 million in 1982. We expect this year to collect over $70 million on defaulted student loans.

But there is more to do, and we believe that we can effect even greater debt collection through several legislative efforts that we plan to propose in the very near future.

I know that it's a technical program, but the loan program is the one that I think has the greatest potential for waste, fraud, and abuse in the future, and the one I think S. 150 is attempting to direct its activities.

Right now, under the current program, loan checks when issued are made available directly to the student. We find that that has resulted in duplicate payments, with students leaving one institution and attending another institution while is the same year being able to borrow the same amount of money. However the law requires that only $2,500 may be borrowed in 1 year. In additional, there exists the potential for a student to receive a check at home and never showing up at the institution. When this occurs, the loan goes immediately into default, and we have the burden of trying to collect it. We will propose legislation that will make the loan check payable both to the student and to the institution. In that way, the check would be sent to the institution, a copayee situation would be set up, and the student would have to show up for class in order to collect the loan.

A second major problem we have is that our guarantee agencies in all 50 States, 8 trust territories, and other entities that have agencies do not have the ability to share information with credit bureaus. We would ask for legislation for them to do that.

Currently, under the law, a student is able to have their loan refund checked against only activities or receivables at one institution. If they were to go into a different program or go to a different institution, they would in fact not be able to have us offset that. With the legislation we would ask for to broaden student eligibility, we would ask that the student may not, under any condition, receive Federal financial aid if a student owes a refund on a grant or is in default on a loan made under title IV at any institution and not just the institution where they happen to be enrolled.

And finally, we would ask that the 6-year Federal statute of limitations, which now exists for guarantee agencies on filing suit for collections be extended, so that the recovery potential would be greater.

In addition to this, I don't know if you are familiar with S.1688 which has just been introduced and supported by the Department of Justice. It provides authority for Justice to contract with private attorneys to litigate cases. We now don't have that authority. All litigation is handled directly by the Department of Justice.

In terms of your letter of invitation to comment on S. 150, given what we have heard from the witnesses from IRS and Treasury this morning, I think it is appropriate that we should defer to

them. I would, however, say that the concept of what you are trying to do is very acceptable to the Department of Education and very laudable.

We will be responsive to any questions you might want to ask about the bill or about the Department of Education's collections efforts.

Thank you.

Senator GRASSLEY. You have already responded to one or two of the questions I was going to ask, through your testimony, but I will continue with other questions unanswered.

In your view, would providing the IRS with the authority to collect defaulted student loans be effective in collecting your current debts?

Dr. ELMENDORF. We believe that the concept of having any other mechanism would be supportable; however, we do find, in terms of what we have heard and what we know, that there are several technical problems with the bill as constructed. And understanding that there is a study to come in October which more or less pilots what we would do, I would advise waiting until we have the results of that study to see what the effectiveness might be of an offset.

Senator GRASSLEY. Then at this point it would be difficult for you to say whether or not this approach would be more cost effective than your current approach?

Dr. ELMENDORF. Yes, sir.

The Government Debt Collection Act, which passed last session, permits Federal agencies to obtain the names and addresses of delinquent debtors from the IRS files. Have you used this new tool in collecting delinquent student loans?

Dr. ELMENDORF. Yes, we have, and I would perhaps let Mr. Reynolds give you some more detail on that.

Senator GRASSLEY. OK. And while you are responding to that, then, has it been effective, and has it been cost effective?

Mr. REYNOLDS. Mr. Chairman, we were doing income tax address checks under an interagency agreement since 1976. The Debt Collection Act gave that authority to all government agencies. In the years that we have been using it, we have found it to be extremely effective in updating old addresses of borrowers.

We have, in fact, a hit rate where, when we give IRS the social security number of the borrower, they are coming back to us in about 65 percent of the cases, with a good address. That, then, enables us to contact the debtor and in about 34 percent of those cases convert those cases to repayment status. So we think it has been very cost effective.

Senator GRASSLEY. Is this a better collection technique than referring the case to the IRS to do the collection?

Dr. ELMENDORF. We haven't had the experience of referring the case to the Department of Treasury or any other agency. We have been responsible for collections within our own agency. I must, however, tell you that there is such a progression in the collection effort that starts with the loan going immediately into default, being first collected on either by the institution, if it's a National Direct Student Loan, or the State agency. We pay the State agencies 30 cents on the dollar to collect defaulted student loans for the

Government. We then have those cases that can't be collected referred back to the Department.

We make an attempt in our three major regions—San Francisco, Chicago, and Atlanta—to collect using Federal collectors. We have about 408 Federal collectors. We use the proceeds from collections to pay the cost for those collectors so that we can continue the effort. It costs us about $10.5 million a year to do that.

We then refer the paper that can't be collected by Federal collectors to the private collectors. We pay anywhere from 28 cents to 40 cents on the dollar to get that paper collected.

So we have the very worst paper in our portfolio going to the private collectors, as a last resort. So we have a number of mechanisms right now that are in effect, and we feel, with the additional tools that Congress has given us, we can be even more effective.

Senator GRASSLEY. These two contracts you referred to that you just made agreement with, then it's just at this last stage, what you refer to as the last resort. That's what they've contracted to collect?

Dr. ELMENDORF. Yes, sir. We make every attempt, either directly from the institution where the loan originated, from the State agency where the loan originated, from the Government as a last collector, and then the private collector as the one that gets the residual paper.

Senator GRASSLEY. And that cost to the Government is directly related to the dollars they collect, so they get 26 cents?

Dr. ELMENDORF. Out of the dollars that they collect.

Senator GRASSLEY. OK. And if they don't collect dollars, they get nothing? There is not even any overhead costs or anything?

Dr. ELMENDORF. That's absolutely correct.

Senator GRASSLEY. How does that percentage compare to what the same private sector agencies might get for collecting a private sector debt?

Dr. ELMENDORF. We understand, although we don't have any specific study on this, that between one-third and 50 percent is the rate charged by private sector collectors for other types of debts. So we feel that we are in the range, in fact below the range, in terms of what we pay on student loans.

Senator GRASSLEY. What is the percentage of that debt that can be collected, then, from this last-resort classification?

Dr. ELMENDORF. We will collect in the neighborhood of $70 million this year. We expect that about a third of that will come from the private collection source, and they will take about a third of that in average commissions from that which they collect. But we still anticipate $70 million this year, which is an increase of $15 million over last year.

Senator GRASSLEY. How many dollars worth of outstanding debt is in that last-resort category?

Dr. ELMENDORF. We have referred $640 million, total value of the portfolio, to them. Now, they are in the proces of breaking that down and working the paper, as we call it.

Senator GRASSLEY. OK.

And I don't suppose you've got any way of estimating how much of that $640 million you might get over a period of whatever years?

Dr. ELMENDORF. We did a pilot study in San Francisco before we contracted out the business of last resort paper, and I believe the record on that was that we got back 10 percent of everything we sent out there, keeping in mind that that is the paper that is the most difficult type of paper to collect.

Senator GRASSLEY. Then, what percentage of the total amount due is in that category of last-resort?

Dr. ELMENDORF. We will probably put out 846,000 accounts over 3 years, worth about $1.2 billion.

Senator GRASSLEY. OK. Well then, I guess my question is, what's that $1.2 billion compared to?

Dr. ELMENDORF. It's $1.2 billion of about $3 billion totally, keeping in mind that the States are collecting, that the institutions are collecting, and that the Government is still collecting the balance of the paper.

Senator GRASSLEY. Those are all of the questions I have. I thank you very much for your participation.

Dr. ELMENDORF. Thank you, Mr. Chairman.

Senator GRASSLEY. We would invite you to continue to be in touch with us if you have any further ideas on this legislation.

Dr. ELMENDORF. Thank you.

Senator GRASSLEY. Our next witness, who is testifying for the General Accounting Office, is John Simonette. He is an Associate Director of Accounting and Financial Management. He is in charge of operation and auditing of the Government's accounting systems. He has worked for the General Accounting Office for 20 years and has served in his present capacity for 4 years.

Would you introduce your associate?

Mr. SIMONETTE. Yes, sir, Mr. Chairman.

STATEMENT OF JOHN SIMONETTE, ASSOCIATE DIRECTOR, ACCOUNTING AND FINANCIAL MANAGEMENT DIVISION, GENERAL ACCOUNTING OFFICE, WASHINGTON, D.C.

Mr. SIMONETTE. We are pleased to be here to discuss with you the IRS offset concept. With me this morning is Mr. Darby Smith, senior accountant, Accounting and Financial Management Division.

My prepared statement contains background information on the magnitude of the Federal debt, as well as recent actions taken by the Congress and the administration to stem the growth of debts owed the Government. In the interest of time, I will move directly to the IRS offset issue.

Senator GRASSLEY. Please.

Mr. SIMONETTE. Although significant accomplishments have been made in the collection area, continued emphasis is needed to reduce the increase in delinquent debts owed the Federal Government. One means available is the use of offset of delinquent debts against Federal tax refunds due to debtors.

In March 1979 we reported to the Congress that, of a sample of 613 terminated debts totaling $431,000, up to $153,000, or 36 percent, could have been collected over a 2-year period by reducing the debtors' tax refunds. We recommended that on a test basis delinquent nontax receivables be collected by reducing future income

tax refunds due the debtors. Such offsets would be made only after procedures to protect the debtors' rights to due process had been instituted. The proposal in the fiscal 1980 IRS appropriation bill to fund 30 positions for such a test was not adopted; however, several Members of Congress were interested in pursuing legislation on this point.

In response to a request from the chairman of the Legislative Appropriations Subcommittee, Senate Committee on Appropriations, we reported in July 1980 that in 1979 alone the State of Oregon was able to collect by offset from tax refunds over $2.4 million in delinquent debts at a cost of about $200,000. While at the same time establishing strict controls to insure the debtors' rights to due process are protected and that tax refunds are not arbitrarily offset.

In testimony before the Senate Governmental Affairs Committee on April 23, 1981, the Director of Oregon's Department of Taxation reported that collections for 1980 were $3.7 million, at a cost of less than $300,000.

We believe effective arrangements for using IRS offset to collect nontax debts could be worked out on the basis of interagency agreements between IRS and the Federal agencies wishing to refer debts for offset, with the Attorney General having a consultation role in the development of such agreements.

Our support of the IRS offset should not be interpreted as a recommendation that IRS become a debt collection "clearinghouse." Debt collection is the primary responsibility of each Federal agency, and it is incumbent on top management to establish debt collection as a priority and insure that the initiatives underway and planned are successfully implemented.

This concludes my brief remarks, Mr. Chairman. We would be happy to respond to any questions that you have.

[The prepared statement of John F. Simonette follows:]

U.S GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

FOR RELEASE ON DELIVERY
EXPECTED 9:30 A.M. EDT
FRIDAY, SEPTEMBER 16, 1983

STATEMENT OF
JOHN F. SIMONETTE
ASSOCIATE DIRECTOR
ACCOUNTING AND FINANCIAL MANAGEMENT DIVISION

BEFORE THE
SUBCOMMITTEE ON OVERSIGHT OF THE
INTERNAL REVENUE SERVICE
COMMITTEE ON FINANCE
UNITED STATES SENATE

ON
OFFSET OF FEDERAL TAX RETURNS

Mr. Chairman and members of the Subcommittee, thank you for the opportunity to appear before you to discuss offset of delnquent debts against Federal tax refunds due to debtors. Before discussing the offset issue, I would like to present the Subcommittee with some background information on the magnitude of debts owed the Federal Government and the efforts underway to stem this growth.

Debts owed the Government are enormous and growing each year, with billions of dollars delinquent. Federal agencies reported that, at the start of fiscal 1982, receivables due from U.S. citizens and organizations exceeded $180 billion, over $33 billion of which was delinquent. By the end of fiscal 1982, these amounts had further increased to approximately $200 billion and $38 billion, respectively, with nontax delinquencies totaling about $14 billion.

To stem the continued growth in these numbers, the Congress and GAO have long called for strengthened debt collection. We

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have reported that the Government was not doing an effective job of accounting for and collecting its debts. Recognizing the need for improved financial management, the Administration made debt collection a management priority.

ADMINISTRATION'S EFFORTS TO IMPROVE DEBT COLLECTION

In response to our work and to congressional interest in improved Government debt collection, the Debt Collection Project was established in August 1979 within the Office of Management and Budget (OMB) for the purpose of identifying and recommending solutions to Government-wide problems which impede agency collection efforts. The Debt Collection Project, which was made up of private and public sector representatives, reviewed Federal agencies' debt collection policies and procedures. The programs reviewed in these agencies accounted for 95 percent of the debt owed the Government. In January 1981, the Project issued its "Report on Strengthening Federal Credit Management" which included a series of recommendations for strengtheing credit management and debt collection.

Recognizing the need for improved financial management, the administration made debt collection a management priority. In an April 23, 1981, memorandum, the President directed the heads of executive branch agencies and departments to develop and implement an aggressive debt colletion program by:

--Designating an official with responsibility and authority for debt collection. Twenty-four major departments and agencies have designated such an official.

--Reviewing current debt collection issues and preparing action plans for improved debt collection, to be approved by OMB.

--Submitting periodic progress reports to OMB on the status of planned actions.

OMB is responsible for monitoring agency efforts to comply with the President's directive and for providing a focal point in the debt collection area.

PASSAGE OF THE DEBT COLLECTION ACT OF 1982

In addition to establishing the policies governing the debt collection initiative and overseeing agency corrective actions, OMB served as the administration's focal point for the Debt Collection Act of 1982. On April 23, 1981, the Director of OMB, in testimony before the Senate Committee on Governmental Affairs, proposed comprehensive legislation to eliminate certain disincentives in the Government's debt collection process; to make available essential collection tools and techniques commonly used in the private sector; and to provide for increased efficiency and effectiveness in the way the Government grants credit and services and collects its receivables. OMB worked closely with the Congress and on October 25, 1982, the President signed into law the Debt Collection Act of 1982. Among other things, the act

--allows agencies to disclose information about an individual's debt to credit bureaus except when a debt arises under IRS or SSA regulations;

--authorizes agencies to collect overdue payments from Federal employees through deductions from their paychecks;

--permits agencies to disclose to debt collection contractors current addresses of individuals owing money to the Government;

--authorizes the IRS to disclose to a requesting agency whether an applicant for a Federal loan has a delinquent tax account;

--provides a 10-year period for agencies to collect debts by administrative offset;

--requires agencies to charge a minimum rate of interest, as well as penalties and administrative charges on deliquent nontax debts unless otherwise provided for in contract, statute, or agency regulations; and

--authorizes agencies to contract for debt collection services.

Implementation of the act will undoubtedly increase collections by giving Federal agencies tools already widely used in the private sector.

OFFSET OF FEDERAL TAX REFUNDS

Although significant accomplishments have been made in the debt collection area, continued emphasis is needed to reduce the increase in delinquent debts owed the Federal Government. One means available is the use of offset of delinquent debts against Federal tax refunds due to debtors.

Federal tax refunds are routinely made to many individuals who have not paid debts owed the Government. In March 1979, we reported to the Congress that of a sample of 613 terminated debts totaling $431,000, up to $153,000, or 36 percent, could have been collected over a 2-year period by reducing the debtors' tax refunds. We recommended that, on a test basis, delinquent nontax receivables be collected by reducing future income tax refunds due the debtors. Such offset would be made

only after procedures to protect the debtor's rights to due process had been instituted. To protect the debtor's rights to due process the agency referring a debt for offset would be required to

--establish the debts validity by giving the debtor ample opportunity to dispute the Government's claim,

--notify the debtor that the receivable was being transferred to IRS for collection,

--give the debtor an opportunity to request a hearing on the offset, and

--notify the debtor when the debt was collected by offset.

IRS expressed reservations about the desirability and practicality of such a program when balanced against the value of concentrating IRS resources and expertise on the administration of tax laws as well as the potential negative effect on the taxpayer withholding system. A proposal in the fiscal 1980 IRS appropriations bill to fund 30 positions for such a test was not adopted.

Several members of Congress, however, were interested in pursuing legislation on this point. In response to a request from the Chairman of the Legislative Appropriations Subcommittee, Senate Committee on Appropriations, we reported in July 1980, that in 1979 alone, the State of Oregon was able to collect by offset from tax refunds over $2.4 million in delinquent debts at a cost of about $200,000. While at the same time, establishing strict controls to ensure that debtor's rights to due process are protected and that tax refunds are not

arbitrarily offset. In testimony before the Senate Governmental Affairs Committee on April 23, 1981, the Director of Oregon's Department of Taxation reported that collections for 1980 were $3.7 million at a cost of less than $300,000. In supporting this type of offset we wish to emphasize that the necessary safeguards to protect debtors against arbitary offset actions can and must be instituted, and the offset procedures should be thoroughly tested prior to full implementation.

We believe effective arrangements for using IRS offset to collect nontax debts could be worked out on the basis of interagency agreements between IRS and the Federal agencies wishing to refer debts for offset, with the Attorney General having a consultation role in the development of such agreements. This would clearly mandate IRS to follow through with an offset program to the extent appropriate procedures could be worked out. The interagency agreement would provide a mechanism for resolving due process and other procedural issues. We anticipate that the Attorney General could contribute to resolving differences should the referring agency and IRS be unable to agree on procedures.

We are aware that the AFDC program provides for the collection of delinquent child support payments through use of IRS offset. As with any new program, certain problems are going to occur and must be resolved in order for it to operate in an effective, efficient, and economical manner. Although the AFDC program is for the collection of non-government debts, we believe the lessons learned and problems encountered should be

carefully considered in developing an offset program for the collection of debts owed the Federal Government.

Our support of the IRS offset should not be interpreted as a recommendation that IRS become a debt collection "clearinghouse". Debt collection is the primary responsibility of each Federal agency. It is incumbent upon top management to establish debt collection as a priority and ensure that the initiatives underway and planned are successfully implemented.

This concludes my statement. I will be happy to answer any questions you or other members may have.

Senator GRASSLEY. I know that your office has traditionally been concerned with the erosion of taxpayers' compliance with our revenue laws. Do you have any concern that the refund offsets and debt referral to the IRS will undermine compliance? I know you are aware of the testimony from the Treasury Department on this point.

Mr. SIMONETTE. Yes, sir. We certainly appreciate the potential for such an adverse effect. This point was also raised in 1979 by IRS when we asked them to comment on our report to the Congress.

What we are advocating and what IRS offset would do is to offset tax refunds for a select group of people who have not paid their debts owed the Federal Government affect. We do not envision the IRS offset would affect the general taxpayer. In other words, there are people who for one reason or another have chosen not to pay undisputed debts owed to the Government, and the use of IRS offset is a viable way to collect at least some of that money.

We are not talking about affecting the general taxpayer. We have not seen any evidence, and the IRS appropriately pointed to this today, there is no evidence to indicate the impact—if any—that IRS offset would have upon the voluntary tax compliance program. We understand that IRS is preparing a study that may have some information to that effect.

Senator GRASSLEY. Well, considering that potential study, I guess I would still ask—and this question comes out of the frustration that I feel because we can't quantify the potential danger to voluntary compliance—whether or not your organization might be working for ways to measure whether or not these initiatives would affect voluntary compliance.

I know the IRS, that would be their main concern; but as you have worked on these theories, is there any way that they can be quantified?

Mr. SIMONETTE. To my knowledge, Mr. Chairman, there would be no way that the possible impact could be quantified at this point, since there has not been extensive use of the offset program to collect Federal debts.

What needs to be done is to implement the program as we recommended in our 1979 report. The program should be implement on a test basis—to determine how it could best be worked out on a governmentwide basis. Also a test program would help identify major problems and hopefully any quantification of those, including the effect it might have on the withholding system.

The program for child support payments is the only large effort that has been done so far using IRS offset. We are in a situation where we lack the evidence, needed to make such a determination.

Senator GRASSLEY. OK.

Mr. SIMONETTE. We have been advised, at least in the case of Oregon, that they have not experienced any significant effect on the withholding system. They have been using the offset program, since the early 1970's.

Mr. SMITH. As Senator Percy pointed out, 17 other States are now offsetting tax refunds and have not experienced any effect on the withholding system.

Senator GRASSLEY. In the case of Oregon, do you know whether that statement is based on a perception that some tax administrator might have? Or is it based on some scientific analysis?

Mr. SIMONETTE. I am not sure; do you know, Darby?

Mr. SMITH. As Mr. Simonette pointed out, in the hearing that was held by Senator Percy in April 1981, the representatives of the State of Oregon, stated that there was no adverse effect. I do not know the basis for his statement.

Senator GRASSLEY. You know, I am aware that in the past several years the General Accounting Office has been critical of how IRS might divide up their resources to accomplish some if its responsibilities.

Since the provisions of the legislation before us require the IRS to use scarce resources for functions other than their main purpose which is tax collection, from your standpoint and from your analysis of the IRS's past allocation of resources, do you feel that they would be using their resources in a cost-efficient way if they were compelled to pursue these responsibilities in yet more comprehensive ways than required under existing law has?

Mr. SIMONETTE. We believe that this would be an effective use of IRS resources. However, there may be a need for additional funds for additional positions, for computer programing and other procedures that may have to be implemented. We do not have a precise figure at this time, but as was pointed out earlier, the 1980 appropriations bill did provide for 30 positions.

We continue to believe that even if IRS would require additional positions and additional funds to carry an offset program out, that we think, given proper implementation, that this would be a cost-effective approach, and that a substantial amount of money could be collected.

Senator GRASSLEY. OK. I appreciate that very much, and I'm sure the IRS will even appreciate it more.

We appreciate your testimony, and I look forward to our continuing to work with you as we decide what to do in this area.

Mr. SIMONETTE. Thank you, Mr. Chairman.

Senator GRASSLEY. Thank you both very much.

Our next witness is a panel of three: Dan Copeland, Bonnie Becker, and John Abbott. I would ask those three to come at this time, and I would like to introduce John Abbott as a person testifying for the National Reciprocal Family Support Enforcement Association, currently director of the Office of Recovery Services for the University of Utah.

And of course I would like to say that the Utah program is nationally recognized for their high rate of recovery in ADC collections.

Dan Copeland is testifying for the National Council of Child Support Enforcement Administrators, of which he is currently the president. He is a member of the executive board of this association, and he has served with the Department of Revenue for the State of Alaska.

Bonnie Becker is testifying as the director of the Office of Child Support Enforcement for the State of Minnesota. She has been with that enforcement agency since its creation in 1975, and prior to that she spent 5 years with the Hennepin County Child Support Enforcement Office.

I would ask you to proceed in the way I introduced you.

STATEMENT OF JOHN P. ABBOTT, PRESIDENT-ELECT, NATIONAL RECIPROCAL FAMILY SUPPORT ENFORCEMENT ASSOCIATION, DES MOINES, IOWA

Mr. ABBOTT. Thank you, Mr. Chairman. It is indeed an honor to appear before this subcommittee today to address some of the issues surrounding the Federal tax refund offset program.

As you mentioned, I am John Abbott. I am the director of the office of recovery services for the State of Utah, and also president-elect of the National Reciprocal Family Support Enforcement Association.

As you may know, the NRFSEA organization is the largest national forum for child-support practitioners, and we have just concluded our annual meeting in St. Louis, Mo. During the course of our deliberations the IRS intercept program was extensively discussed, and I will be reporting to you on some of the results of those discussions as well as the position of the State of Utah regarding the tax intercept program.

First, however, I would like to briefly address the scope of the problem. As you may know, more than 15 million children are living in families where the father is absent. Close to one-third of those are living in poverty. More than half of the families who should receive court-ordered child support do not receive full payment; thus, depriving children of billions of dollars in support money owed each year.

In many of these cases the unfortunate children are left without the necessities of life. It is a shocking fact that over half of all women who receive child support receive less than they are entitled to. In fact, 28 percent of these women and their children receive no payments whatsoever.

The children in this country are in fact owed over $4 billion annually from delinquent parents. This situation is clearly unacceptable. The IRS refund offset program, however, has made significant

inroads over the last 2 years to at least make a dent in this problem.

You have already heard testimony from Commissioner Egger and Mr. Schutzman about the success of the program over the first 2 years, so I won't elaborate on that. However, clearly, with almost $340 million brought into State and Federal coffers as the result of the intercept program, we believe the success speaks for itself.

Obviously there have been problems, but in our view they are to be expected with a program of this magnitude, which at this point in time has affected over 600,000 taxpayers who have basically failed to live up to their child-support obligations.

The impact on the Internal Revenue Service system has also no doubt been significant. As Commissioner Egger has pointed out. However, the IRS has been reimbursed at the rate of $17 per offset during the first year and $11 per offset during the second year. These sums of money obtained hopefully have reimbursed the IRS for the costs of providing this service.

We do appreciate the IRS's cooperation and their willingness to work with the States and the Office of Child Support Enforcement at the Federal level to make the program the success it has been to date.

From an individual State point of view, I would like to point out that Utah has been able to collect, through the IRS intercept program, almost $6 million in the past 2 years—and that's a relatively small State. Without the IRS program, most of this money would have gone uncollected, and the State and Federal Government would have been left without the reimbursement for that portion of the AFDC money that was paid out.

I would further point out that 87 percent of the reason for AFDC eligibility in the first place is the lack of or the inadequate payment of child support.

We appreciate the success of the program and the increased collections that have been made; however, we believe that the program should be conisdered for future expansion in several areas:

First, there are currently 1.5 million non-AFDC cases serviced by the title IV-D program. The majority of these individuals are mothers with children living barely above the AFDC grant level. Many States have made it a priority to service this caseload, to prevent these individuals from falling dependent upon AFDC assistance. Due to the resounding success of the AFDC offset program, we would urge this committee to fully consider expanding this service to include the non-AFDC caseload. This could be done quite easily on non-AFDC cases where the arrearage has been reduced to a judgment or a central registry record is available to document the lack of payment.

We certainly do not want to get into a situation where we are intercepting tax refunds when the child-support debt is current. Therefore, we recommend that only cases meeting the above criteria be accepted for the offset.

We do have some procedural concerns with the 1040-X refund process where the obligee's present wife can amend the tax return using the 1040-X process for up to 3 years and go back and obtain her share of the tax refund. If the tax refund has already been forwarded to the obligee, any adjustment definitely will create some

problems. However, in spite of this difficulty, we urge the committee to recognize that the receipt of child support through this system is often the difference, for non-AFDC families, of AFDC dependence or financial independence.

We would further encourage the committee to include in their offset provisions moneys owed to the State and Federal Government from individuals found guilty of welfare fraud. We believe this should include AFDC, medicaid, and food stamp related fraud. Again, the amounts owed should be reduced to a judgment by the courts before the offset could occur.

I would like to point out that in Utah we have had a State tax intercept program for 6 years. We found this program to be extremely successful. We have, in fact, used it to collect child support for non-AFDC cases as well as welfare fraud cases. We would encourage the committee to expand the IRS offset to include these kinds of activities.

Additionally, expanded enforcement through the 6305 process should be seriously considered by the committee, and we would urge you to look into expanding the access and streamlining the procedures for this program.

We should also, I believe, eliminate this as a last resort measure. We believe that the regional offices of the office of child support enforcement could be responsible for central monitoring to eliminate duplications of effort.

We believe that the use of this process, in combination with ongoing State enforcement remedies should be permissive.

In summary, Mr. Chairman, we believe that the IRS tax offset program has been a tremendous success and should be further expanded to help address the needs of non-AFDC families and other areas where a public debt is owed. The bottom line, as Senator Percy has so eloquently pointed out this morning, is the molding of an ethic which makes individuals responsible for their actions and obligations, be it welfare fraud, child support, or other government debts that are owed.

I thank you for this opportunity to testify.

[The prepared statement of John P. Abbott follows:]

STATEMENT OF TESTIMONY

UNITED STATES SENATE

COMMITTEE ON FINANCE

Subcommittee on Oversight of the

Internal Revenue Service

SEPTEMBER 15, 1983

NATIONAL RECIPROCAL AND FAMILY SUPPORT ENFORCEMENT ASSOCIATION

By John P. Abbott

UNITED STATES SENATE

COMMITTEE ON FINANCE

Subcommittee on Oversight of the

Internal Revenue Service

SEPTEMBER 15, 1983

Mr. Chairman, it is an honor to appear before this Subcommittee today to address some of the issues surrounding the federal income tax refund offset program. I am John P. Abbott, Director of the Office of Recovery Services for the State of Utah and also President-elect of the National Reciprocal Family Support Enforcement Association. NRFSEA is the largest national forum for child support practitioners and we have just concluded our annual meeting in St. Louis, Missouri. During the course of our deliberations, the IRS intercept program was extensively discussed and I will be reporting to you on the results of those discussions as well as the position of the State of Utah regarding the tax intercept program.

First, however, I would like to briefly address the scope of the problem. As you may know, more than 15 million children are living in families where the father is absent. Close to one-third of those are living in poverty. More than half of the families who should receive court ordered child support do not receive full payment, thus depriving children of billions of dollars in support each year. In many of these cases, the unfortunate children are left without the necessities of life. It is a shocking fact that over half of all women who receive

child support receive less than they are entitled to. In fact, 28% of these women and their children receive no payments whatsoever. The children in this country are, in fact, currently owed over $4 billion from delinquent parents. This situation is clearly unacceptable. The IRS refund offset program, however, has made significant inroads over the last two years to at least make a dent in the arrearages owed on the AFDC cases throughout the country. In the first year of the program, 273,000 cases were processed, which yielded $169 million in collections. During the second year of the program, which is the year we are now in, $170 million has been collected thus far. Clearly, with almost $340 million brought into the state and federal coffers as a result of the intercept program, its success speaks for itself. Obviously, there have been problems, but in our view, they were to be expected with a program of this magnitude affecting at this point in time some 600,000 taxpayers who have failed to live up to their child support obligation.

The impact on the Internal Revenue Service system has no doubt been significant. However, it should be pointed out that IRS has been reimbursed at the rate of $17 per offset during the first year and $11 per offset during the second year. The sums of money obtained through the offset fees, in our opinion, have adequately reimbursed IRS for the costs of providing this service. We do appreciate the Internal Revenue Service's cooperation and willingness to work with the states and the Office of Child Support Enforcement in making this program the success it has been heretofore.

From an individual state point of view, Utah has been able to collect, through the IRS intercept program, almost $6 million in the past two years. Without the IRS program, most of this money would have gone uncollected and the state and the federal government would have been left without reimbursement for that portion of the AFDC money that was paid out. I would like to point out that 87% of the reason for AFDC eligibility is the lack of or inadequacy of child support payments. While we appreciate the success of the program and the increased collections that have been made, we believe that the program should be considered for future expansion in several areas.

First, There are currently 1.5 million Non-AFDC cases serviced by the Title IV-D program. The majority of these individuals are mothers with children living barely above the AFDC grant level. Many states have made it a priority to service this case load to prevent these individuals from falling dependent upon AFDC assistance. Due to the resounding success of the AFDC offset program, we would urge this Committee to consider expanding the service to include the Non-AFDC case load. This could be done quite easily on those Non-AFDC cases where the arrearage has been reduced to a judgment or a central registry record was available to document the lack of payment. We certainly do not want to get into a position where we are intercepting tax refunds when the child support debt is current. Therefore, we recommend that only cases meeting the above criteria be accepted for offset. We do have procedural concerns with the 1040X process. The obligee's present wife can amend the tax return using the 1040X process for up to three years to obtain her share

of the tax return. If the tax refund has already been forwarded to the obligee, any adjustment would definitely create a problem. In spite of this difficulty, we urge the Committee to recognize that the receipt of child support through this system is often the difference for Non-AFDC families of AFDC dependence or financial independence.

We would further encourage the Committee to include in their offset provisions monies owed to the state and federal government from individuals found guilty of welfare fraud. We believe this should include AFDC, Medicaid, and Food Stamp related fraud. Again, the amounts owed should be reduced to a judgment before the offset could occur.

I would like to point out that in Utah, we have had a state tax intercept program for six years. We have found this program to be extremely successful. We have, in fact, used it to collect child support for Non-AFDC cases as well as welfare fraud cases. We would encourage the Committee to expand the IRS offset to include these activities. Additionally, expanded enforcement through the 6305 process should be seriously considered by this Committee. We would urge the Committee to:

1. Expand access and streamline procedures for IRS 6305 process.
2. Eliminate last resort restriction.
3. OCSE regional offices will be responsible for central monitoring and reporting of those collections to avoid duplication of effort.
4. Permit the use of this process in combination with ongoing state enforcement remedies.

In summary, we believe that the IRS tax offset program has been a tremendous success and should be further expanded to help address the needs of Non-AFDC families and other areas where a public debt is owed. The bottom line is the molding of an ethic which makes individuals responsible for their actions and obligations be it welfare fraud or child support owed.

Senator GRASSLEY. Before we go on, I would like to have you clarify a point for me. I missed it, but later on you said you referred to 'above criteria' in which this procedure would be instituted. What are those criteria?

Mr. ABBOTT. OK.

Those criteria were the fact that the non-AFDC program should be included in the offset process. But in order to safeguard that process, the amounts owed should be reduced to a judgment, either through a court order or an administrative order.

Second, as another option, they should be a part of a central registry file where that information on the amount of the arrearage could be documented, so that we would have a sum-certain that we were certifying to, and that there would be no question about the fact that the child support had not been paid.

Senator GRASSLEY. In the legislation that I have sponsored, we would put resources into that central registry, greater resources.

Mr. ABBOTT. Yes, sir. And we are certainly anxious to see that legislation proceed.

Senator GRASSLEY. Mr. Copeland?

STATEMENT OF DAN COPELAND, PRESIDENT, NATIONAL COUNCIL OF STATE CHILD SUPPORT ENFORCEMENT ADMINISTRATORS, ANCHORAGE, ALASKA

Mr. COPELAND. Thank you. Good morning.

I am Dan Copeland, president of the National Council of the State Child Support Enforcement Administrators. I also serve as the director of the Alaska State Child Support Enforcement Agency. Our national council includes the operational head of each State child support agency.

The council is committed to the principle that all enforcement tools should be available equally to all child support cases. This should include AFDC and non-AFDC or instate and interstate casework. It is imperative that all absent parents recognize that all collection methods will apply to their own individual obligation to pay without regard to the economic status or location of the custodial parent with their child.

Many of the bills now facing Congress include a purpose statement that would imply this type of universal approach. The offset of IRS refunds for all cases rather than just the AFDC situations would be one of the most tangible statements made in this regard. In opening the IRS refund offset process to the non-AFDC caseload, it must be recognized that this has the potential for greatly expanding the number of custodial parents that will want to use the child-support system. Many custodial parents that have given up any thought of ever receiving any child support will now see this process as one last hope. It is important that we make sure that their hopes are not lost.

However, many substantial barriers stand in the way of allowing the IRS process to work to its fullest extent. The first and most significant factor is the basic program intent. While child support and the non-AFDC caseload is currently receiving a lot of attention in Congress and in the States, many of the State and local political jurisdictions need assurances that child support services and not

governmental AFDC reimbursement is the program objective. This very basic message, that child support is to be viewed as a service to the public, will take time to be accepted. Acceptance of this will have a substantial impact on how the State and local jurisdictions implement the process of offsetting IRS refunds for non-AFDC cases. Once the basic program intent is established nationwide, down through each county and local child support operations, the offset process will become one of the most effective tools available.

The success of the AFDC IRS offset refund process is one of the driving factors in the push to expand the program to include the non-AFDC caseload. During fiscal year 1982, better than 547,000 AFDC arrearage cases were submitted to IRS, and 260,000, or 48 percent, of these cases produced an actual cash response. In this first year of operation, over $160 million was collected and distributed to the State and Federal Government. The figures are indicators of success, but a more important fact is that many cases that had proved to be totally uncollectable in the past now produced amazing results.

In many instances the process of offsetting the refunds is declared to be a simple and inexpensive process. When compared to some of the routine child support problems, this may be true, but in actual fact there is a considerable effort involved. The States, counties and Federal governments all go through a notice process, which insures due process prior to attachment. Once the notice is sent out on all of the cases, a great number of the absent parents then contact the appropriate agency at the State and local level, and the first attempt is made to work out a payment arrangement. The phone calls and office contacts continue to create extensive workload requirements at the local levels Naturally, this process will find some cases where the arrearages were incorrect, and adjustments are required. These adjustments are made timely and without serious problems in most cases.

During June of 1982 the Federal Office of Child Support Enforcement conducted a review of selected State 1981 IRS submissions. These reviews were instrumental in refining the process with quality assurance mechanisms, additional pre-offset notices, and quicker deletions or release processes. All indications are that the operations for the next years will be even more effective.

One of the first questions that often develops when the IRS process for non-AFDC cases is developed is whether or not the process will work in the first place. This question is asked because there are numerous problems associated with the non-AFDC caseload that are not common to the AFDC caseload. Doing the IRS offset process on the non-AFDC caseload forces people to recognize these difficult situations on a large number of cases. However, it is important to recognize that each of these problems is a part of every enforcement action on each individual case in that non-AFDC area.

For example, in every instance there is always the possibility that the absent parent has sent the money directly to the custodial parent, and the arrearages as stated are incorrect; if this is the situation, the due process requirements for all seizure actions protect the absent parent with notice and time to respond. This is currently a routine part of every agency that handles any volume of non-AFDC cases. It is used in filing liens, attaching wages, offsetting

State income tax refunds, seizing bank accounts, and will be a requirement in any IRS offset process. While using the IRS offset process for the non-AFDC cases will certainly cause some problems, all of these problems are resolvable and the process certainly should become law.

The real question to be asked is not whether or not a State can operate an IRS non-AFDC intercept process; in actual practice the bottom line question is whether or not the States and local operations have the ability to accept the additional non-AFDC service requirements in all areas that this IRS offset process is going to attract.

Thank you.

[The following was provided for the record:]

National Council of State Child Support Enforcement Administrators

Committee on Finance
Subcommittee on Oversight of
the Internal Revenue Service
Tax Refund Offset Program and S-150
September 16, 1983

Testimony Provided by:
Dan R Copeland
President

Good Morning, I am Dan R Copeland, President of the National Council of State Child Support Enforcement Administrators. I also serve as the Director of the Alaska Child Support Agency. Our National Council includes the operational head of each state child support agency.

The Council is committed to the principle that all enforcement tools should be available equally to all child support cases. This should include AFDC and non-AFDC or instate and interstate casework. It is imperative that all absent parents recognize that all collection methods will apply to their own individual obligation to pay without regard to the economic status or location of the custodial parent with their child.

Many of the bills now facing Congress include a purpose statement that would imply this type of universal approach. The offset of IRS refunds for all cases rather than just the AFDC situations would be one of the most tangible statements made in this regard. In opening the IRS refund offset process to the non-AFDC caseload it must be recognized that this has the potential for greatly expanding the number of custodial parents that will want to use the child support system. Many custodial parents that have given up any thought of receiving child support will see this process as one last hope. It is most important that we make sure their hopes are not lost.

Many substantial barriers stand in the way of allowing the IRS refund offset process to work to its fullest extent. The first and most significant factor is in the basic program intent. While child support and the non-AFDC caseload is currently receiving a lot of attention many of the state and local political jurisdictions need assurances that child support services and not government AFDC reimbursement is the program objective. This very basic message, that child support is to be viewed as a service to the public will take time to be accepted. Acceptance of this will have a substantial impact in how the state and local jurisdictions implement the process of offsetting IRS refunds for non-AFDC cases. Once the basic program intent is established nationwide down through each county and local child support operations, the offset process will become one of the most effective collection tools available.

The success of the AFDC IRS offset process is one of the driving factors in the push to expand the program to include the non-AFDC caseload. During FY 82, better than 547,000 AFDC arrearage cases were submitted to IRS and 262,030 or 48% of these cases produced an actual cash response. In this first year of operation over $166,000,000 was collected and distributed to the state and federal governments. The figures are indicators of success but a more important fact is that many of the cases that proved to be uncollectable in in the past now produced amazing results.

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In many instances the process of offsetting the refunds is declared to be a simple and inexpensive process. When compared to some of the routine child support problems this may be true but in fact there is considerable effort involved. The states, counties and federal governments all go through a notice process which insures due process prior to attachment. Once the notice is sent out on all of the cases a great number of the absent parents contact the appropriate agency to work out payment arrangements. The phone calls and office contact continue to create extensive workload requirements at the local operational level. Naturally this notice process will find some cases where the arrearages are incorrect and adjustments are required. These adjustments are made timely and without serious problems in most cases.

During June 1982 the Federal Office of Child Support Enforcement conducted a review of selected state 1981 IRS submissions. These reviews were instrumental in refining the process with quality assurance mechanisms, additional pre-offset notices, and quicker deletions or releases. All indications are that the operations of the 1982 tax year refund process will be more efficient than the previous year.

One of the first questions that often develops when looking at the IRS offset process for non-AFDC cases is whether or not it can be done. This question is asked because there are numerous problems associated with the non-AFDC caseload that are not common to the AFDC cases. Doing the IRS offset process on the non-AFDC caseload forces people to recognize these difficult situations on a large number of cases as a group. However, it is important to recognize that each of these problems is a part of every enforcement action on each individual non-AFDC case. For example, in every instance there is the possibility that the absent parent has sent the money directly to the custodial parent and the arrearages as stated are incorrect. If this is the case, the due process requirements for all seizure actions protect the absent parent with notice and time to respond. This is currently a routine part of every agency that handles non-AFDC cases. It it is used in filing liens attaching wages, offsetting state refunds, seizing bank accounts, and will be a requirement in any IRS offset process. While using the IRS offset process for the non-AFDC cases will cause certain problems, all of these problems are resolvable and the process should become law.

The real question to be asked is not whether or not a state could operate a non-AFDC IRS offset program. In actual practice the bottom line question is whether or not the states and local operations have the ability to accept the additional non-AFDC service requirements in all areas.

Senator GRASSLEY. Would you proceed?
Ms. BECKER. Yes.

STATEMENT OF MS. BONNIE L. BECKER, DIRECTOR, OFFICE OF CHILD SUPPORT ENFORCEMENT, STATE OF MINNESOTA, ST. PAUL, MINN.

Ms. BECKER. Mr. Chairman, my name is Bonnie Becker, and I'm the director of the Minnesota Office of Child Support Enforcement. I am testifying here today on behalf of that office and of the department of public welfare of the State of Minnesota.

My testimony today will be directed to Minnesota's experiences with State tax refund interception of debts owed to the State, State tax refund interception procedures on nonwelfare families, and Federal tax refund program for delinquent child-support accounts.

Minnesota has had a State tax refund interception program in operation for 3 years. The program is not specific to child-support debts, but rather has included any debt meeting certain requirements which is owed to State or county government since the tax offset program began.

Our statute in Minnesota details the priority in which claims are satisfied. If the interception program is expanded to debts other than child support, we believe that the priority in which claims are to be satisfied should be addressed either in the law or clearly in the regulations. This should help to avoid confusion among the various claimant agencies.

If the tax refund interception process is expanded to debts other than child support, the definition of what specifically comprises a debt and the procedures developed for contested claims become of prime importance.

If the debts of the various claimant agencies have not been reduced to court order or judgment, a contested claims procedure must be in effect to meet due process considerations. Regulations must clearly delineate how contested claims will be dealt with, or we believe due process challenges to the program will prevail.

We believe that before claimant agencies are allowed to submit claims, that their contested claims procedures be reviewed to insure fairness so that the entire process is not jeopardized by one weak link.

We strongly believe that the language addressing interest paid on any wrongfully or incorrectly-applied set-off and data privacy requirements be strictly enforced in any expansion procedures under the act to maintain program integrity.

During the 1982 legislative session in Minnesota, our legislature authorized the withholding of tax refunds to satisfy child support arrearages on nonwelfare cases. This amendment was done in a separate section of our tax statutes, apart from the procedures in place for intercepting refunds on public assistance cases. This procedure was treated separately because refunds on nonwelfare cases are not a debt owed to the State. The order for withholding is granted upon showing to the court that payments were not made when due.

Before a refund is intercepted in our State on a nonwelfare case, there must be a finding of an arrearage by a court in our State.

The issue of accuracy of arrearage amounts certified is the key to consideration of expansion of the program to nonwelfare cases. It is essential that the child support agency know that the arrearages it is submitting are true and correct.

It is our recommendation, therefore, that the expansion of this to nonwelfare cases be made only under the following conditions:

First, that the arrearages have been certified as accurate by the court; or

Second, only those arrearages which accrued during the period that the child support agency is servicing the case be submitted.

Although these procedures will not completely absolve the child support agency of all liability for inaccurate submissions, they certainly show intent by the agency that care was undertaken to assure accuracy in the program.

Language within the statute detailing how joint refund situations will be prorated adds an element of fairness to the program, and we recommend that this be given consideration.

It is difficult to justify why a present spouse should be held liable or accountable financially to a former spouse.

One of the major problem areas in the expansion of the tax refund intercept program to nonwelfare cases is the issue of amended returns. Amended Federal taxes on form 1040-X may be filed by a taxpayer up to 3 years from the date of initial filing. A situation such as follows could not be unusual:

In a nonwelfare case, Minnesota intercepts the $500 tax refund of Mr. Johnson and pays it to the ex-Mrs. Johnson for child support arrearages. Eighteen months later Mr. Johnson files an amended return, 1040-X, which increases his tax liability and reduces the amount of the refund that was already paid to the State of Minnesota. The IRS debits the State to get their money back. The State contacts the ex-Mrs. Johnson who has already spent the $500 on school, books, and clothes for the children. The State has a $500 loss in real dollars.

It is this type of scenario that we wish to avoid. There were technical difficulties in the Federal intercept program in its first year of operation. The IRS, the Federal Office of Child Support Enforcement, and the States have been working diligently to overcome them. This second year of operation should be significant in determining whether the technical difficulties are solvable.

I have worked in the child support enforcement field in a professional capacity for the past 13 years and firmly believe that the Fedreal tax refund interception program is the most effective means available to collect large delinquencies of child support in a cost-effective manner.

If we are truly serious about enforcing the payment of child support in nonwelfare cases, it is imperative that the same remedies be available to nonwelfare cases that are available on cases where public assistance is being furnished.

We support the expansion of the Federal income tax refund interception program to nonwelfare cases and offer our assistance and expertise to its development.

Thank you for the opportunity to appear before you today.

Senator GRASSLEY. OK. I have a few questions, and I would ask any or all of you who have something to contribute to each ques-

tion to join in on the response. There might be some areas where one of you would be more qualified to answer than the others. I would appreciate it if you would take the lead if it is in an area where you have more acquaintance with the subject.

There is no doubt in any of your testimony that you all support the extension of the refund offset program to non-AFDC cases—each of you supported that, with certain criteria and preconditions.

Now, is there any opposition to extension from any administrators in your field, because of the fact that the current program provides an administrative grant of 70 percent of the cost of collecting AFDC grants from the Federal Government? Is there any problem there?

Mr. ABBOTT. Well, as long as the 70 percent Federal funding stays in effect. Of course, there are several bills, including the administration's, which would lower that to 60 percent. But as long as we have that in place, I think we can build the kind of a program that will obviously result if you expand the service of the IRS intercept to non-AFDC. You know, as Mr. Copeland indicated, that is going to cause an onslaught of applications, because many of those individuals out there have exhausted basically all of their remedies, and they are going to come in and say, "Gee, there is a chance now to try to get some of that money back." And it is going to cause a tremendous onslaught of applications for that service.

We believe that it would require a continued commitment by the Senate Finance Committee to the funding level that is now in place, that 70 percent.

Senator GRASSLEY. OK. But you aren't asking for anything additional for this? None of you are, or your associations aren't requesting added funds?

Mr. COPELAND. At this point, sir, I think what needs to be recognized is that over the past 4 or 5 years the program has been—there has been a major attempt to steer the program into the AFDC caseload. The AFDC caseload operates on a profit motive, and so forth, and if that's the intent the profit motive will take and drive the program in and of itself.

In the recent past here, we have had a situation where there has been a change, and there has been, all of a sudden, an entry to where we are going to take the program into the total area of child support—AFDC and non-AFDC. The question out there is, is this intent going to remain? Is the program intent to go into the non-AFDC caseload in a full and extensive way?

The people who have been here to Washington, D.C., have been through a number of hearings, and we see that there is a great interest in going in that direction.

Now, we are going to have to go back out to the local levels, to the county people, to try to convince them that there has been a change, non-AFDC is important. There may be some reluctance to get into the non-AFDC intercept process simply because they are not fully accepting that there has been a change, that the program should be addressing the entire area of child support, that the message will be received strongest via the 70 percent. If that is held in place, and it's established at that 70 percent, it's established for all child support cases, I think that message will be accepted. If there is a reduction in that FFP, I think the message will be sent out

loud and clear that there is a question as to what the program intent is.

Senator GRASSLEY. Bonnie referred to efforts in her State to collect from non-AFDC. In either one of the other two States, did you testify to that effort?

Mr. ABBOTT. Yes, sir. We have been doing that for about 6 years now and found it very successful.

Mr. COPELAND. We do it in the State of Alaska. Probably 75 percent of the collection work that Alaska does ends up being non-AFDC casework. And we intercept all types of State cash distribution programs.

Senator GRASSLEY. And all three of you would label your individual efforts as successful?

Mr. COPELAND. Absolutely.

Senator GRASSLEY. I am talking about non-AFDC.

Mr. COPELAND. For non-AFDC.

It is important to recognize, though, that intercepting anything—a State income tax refund or an IRS income tax refund—is a basic seizure of property. A basic seizure requires due process. You've got to tell an individual, "We think you are delinquent; are you?" and to give him kind of that basic opportunity to say yes or no. And then if he is in fact delinquent, maybe he lost a job, broke his legs, and, you know, et cetera. The judicial process requires that we afford the individual certain opportunity for a hearing.

Senator GRASSLEY. Have there been challenges in any of your State courts on this point, as for instance in the *Sorenson* case at the Federal level?

Ms. BECKER. We had a challenge in Minnesota in the first year of operation of the State tax intercept program, a legal aid challenge, and they went directly to Federal district court, and we did prevail.

We worked—our office, the department of revenue, and the attorney general's office worked directly with the authors in drafting our State legislation, and so due process was a prime consideration. We had notices that were sent, an opportunity to ask for a hearing, and that was the finding that the Federal district court made, that due process considerations were taken.

Mr. ABBOTT. We have had a similar experience, Senator. But I guess the bottom line concern we have—and we haven't had this tested in terms of a non-AFDC intercept with our State program, but the scenario that Mrs. Becker described in terms of somebody coming along 1½ years later, filing a 1040-X, reducing the obligation, and getting a subsequent refund, and then the State kind of left out there holding the bag for $500, is a concern to all of us when we talk about going into the non-AFDC program, and we're really not sure how to handle that or how widespread these amended returns will be.

Senator GRASSLEY. My last question: Mr. Copeland, I sense from your testimony that you have a feeling that the tax offset ought to be used in a wide variety of debts owed. I don't know to what extent your State is involved in widespread affects, but do you two tend to agree or disagree with that sweeping approach, the use of the tax offset? I am talking about beyond welfare and nonwelfare family support issues.

Am I right? You were a little bit all encompassing in your testimony.

Mr. COPELAND. Yes, I was.

Senator GRASSLEY. Do you have any feelings on that from the standpoint of expansions within your States or at the Federal level?

Ms. BECKER. Senator Grassley, our program is 3 years old, and when we went in with the initial legislation we started out general, any debt owed to the State, because it was a belief of the authors that——

Senator GRASSLEY. Other than just family support?

Ms. BECKER. Oh, yes.

Senator GRASSLEY. OK.

Ms. BECKER. Any debt owed to the State or to county government—delinquent property taxes are being submitted, student loans, a variety of other situations where there is damage to State property; this type of thing.

The first year about 85 percent of the claims submitted were child support claims. Other types of claims have increased since then. It hasn't posed any problems.

Senator GRASSLEY. Well, then, your States are considerably ahead of what we are talking about doing here at the Federal level—I mean, as far as the different subject matters that would make use of the income tax refund offset?

Ms. BECKER. We have expanded into other types of debt in our State programs.

Mr. COPELAND. The State of Alaska's program is a little bit different, primarily because the Alaska Child Support Agency is located within the department of revenue, and all we collect is child support. We are completely limited to that, and we really have no entry into any other program at all. We are what they really call "single and separate" by the CFR's.

Senator GRASSLEY. I want to thank all of you for your testimony. I have no further questioning. I would suggest to you that I have benefited very much personally from your experience in this area, and I think it ought to encourage us at the Federal level not to proceed with a lot of fear as we look at other efforts to get at other debt owed.

Thank you very much.

Mr. ABBOTT. Thank you.

Mr. COPELAND. I would like to thank you.

Senator GRASSLEY. Our next witness is Mike Barber. He is testifying for the California District Attorney's Family Support Council, and he is a legal representative there. It is my understanding the functioning of the council within the DA's association is the enforcement of support obligations and the determination of proof of parentage.

Mr. Barber has served the district attorney's office in Sacramento for 16 years.

Mr. BARBER. That is correct.

Senator GRASSLEY. OK. I would ask that you proceed as other witnesses have.

STATEMENT OF MICHAEL E. BARBER, LEGISLATIVE REPRESENTATIVE, CALIFORNIA DISTRICT ATTORNEY'S FAMILY SUPPORT COUNCIL, SACRAMENTO, CALIF.

Mr. BARBER. Thank you, Mr. Chairman.

I want to thank the chairman and the subcommittee for the opportunity to testify, not only on behalf of this subdivision, the DA's association, but the DA's association as a whole.

I want to also perhaps expand a little personal observation, after having listened to the gentlemen from IRS, and their expressed concern about the taxpayer being somehow turned off by this concept. I wonder if they realize that there are taxpayers out there who are deprived of support, taxpayers whose child support is paid up in full, taxpayers who are single taxpayers who really don't want to support somebody else's children or have the risk of that, married taxpayers with intact families like myself whose children seem to need 100 percent of their paycheck, and we live off of plastic, and retired individuals who have supported their families and raised them, who are taxpayers, too, and who do not want to see the threat of welfare dependents created because someone is absconding on their obligation to support their children.

While I have no formal authority to speak for all of those people, I would hope this committee also keeps those taxpayers in mind when it weighs the testimony of the IRS about concerned taxpayers somehow absconding on their taxes as well as their child support.

Senator GRASSLEY. I would support that and say that the perception of fairness of our tax system is the necessary prerequisite of voluntary compliance. I think the perception of unfairness will encourage people not to comply.

Mr. BARBER. Thank you, Senator; I heartily agree.

The refund offset program went into effect at the Federal level in 1982. As you heard, it has been in effect in a number of States, including California, for several years prior to that.

It has been described to you in detail, and I will not go through that detail again, except to say that the results from California have proven to be effective not only in terms of collections but also in reducing the cumulative debt. As I pointed out in my testimony, that cumulative debt has gone down by $45 million in the second year, which would suggest to me that we are cleaning up these cases by the use of this set-off program.

We also know, federally, how much money is now owed; at least we have a ball park figure, $2.5 billion. And while I think there are still some cases out there not being submitted in some of the Eastern States, I think you are getting a much better handle on what is not being paid. It has resulted in obligated parents paying voluntarily the support they ignored. By bringing to their attention the sum due, scores of cases pay off delinquent support. Neither they nor we really wish to be entangled with the Internal Revenue. Notice that they are provides a favorable result.

We have located delinquent parents. We were amazed at the number of parents who have been found to have good jobs yielding substantial incomes, even though parent-locator services had not found them over the years. We have corrected accounting data, finding in some cases where we had made errors and some cases

where money had been paid directly, innocently, but others where the public had in fact been cheated. But we have had problems.

We have seen some dimunition in collections, some on a per case basis as has been testified to here, but I think that the key for that is the cleanup of cases, and also the malaise of the economy. I don't think that we are seeing people reduce their withholding to any significant degree; I just think we are hitting harder cases in the second year.

The administration of the program I think could be improved, dealing with complaints and errors. Frankly, as a local government employee I have some problems with IRS' notices and with the information passed on by IRS in that it's created expectations of instant refund and instant action at the local level, where in fact a transfer of funds takes about 8 weeks from the time IRS sends out a notice.

I might add that local officials are able to get funds to the counties within 4 weeks after a notice is sent out, and thus errors can be corrected much more quickly at the State level through State tax officials than they can through the Federal.

I have listed some of the other problems in my testimony with the Federal notice process, and I will not go through them here, because I know your time is limited. You have been here all morning, and you have been very patient, Senator, and I certainly appreciate it of someone believes that this is a vital and important problem.

Incorrect terminology, though, has been a problem, and the lack of understanding of family law is a deep problem at the Federal level.

IRS personnel were referring at one time to second spouses in these cases in terms that would lead one to believe they were wronged or injured. As we discussed, presently this is an incorrect perception of the role of this individual in the process, but one that resulted in significant negative public perception of the program, and problems for the organization.

We have had to work too closely, I felt, with Federal attorneys and educate them in family law, and created problems for ourselves at the Federal court level that have been resolved relatively simply at the State court level or never even came up because there was established case law covering these particular situations at the local level.

Characterization of the refund is one. Surpisingly enough, there are Federal cases that distinguish the refund from the source from which those funds came from, distinguished them in particular from wages. And yet this had to be, in effect, restated to Federal officials in this area. I have got the cases cited that clearly make that distinction, and there are State cases that parallel them.

The second issue is the need for a hearing prior to seizure of the refunds. Now, I have to differ from Ms. Becker in this case. We have case law in California that makes it clear that once an individual is before a court, and has the support order entered, that is his day in court. There is that procedural protection built into the program, and indeed we have recently enstated in California a garnishment law that permits on an affidavit any cumulative support installments to result in a garnishment order if those support in-

stallments have come through in the last 10 years, based just on an affidavit.

Of course, a timely hearing immediately after seizure must be provided, and we certainly concede that point.

Senator GRASSLEY. You are saying that, under California law?

Mr. BARBER. Under California law, yes, sir.

But that has been tested in our appellate courts, and an ex parte issuance without a prior hearing of a writ has been conceived to meet all constitutional challenges.

Senator GRASSLEY. And you are saying we've got to do that in the Federal cases?

Mr. BARBER. Well, what I am suggesting is that you do not need a second and subsequent hearing before we submit the case. And frankly, if you want to run up the cost of the program that would be the way to do it. I would suggest you avoid that.

These intercepts are claimed to be unfair because in some cases there has been an agreement to reduce the delinquency through a deduction from wages. It should be briefly pointed out that many of these arrangements are simply temporary arrangements to avoid the individual being held in contempt.

Fourth, we have the problem of second wives. This was called to HHS's attention early on in the program, and they were advised to review State laws in terms of marital property. However, confusion on this issue has reigned, and State authorities had to do their homework independently.

In California it was found that community property law made such funds totally available for support obligations. As a consequence, it was a nonissue in California, and presumably in other community-property States, which makes the *Sorenson* decision, to me, inexplicable, because under community property law, at least as practiced in California, Mrs. Sorenson's share of that refund should have been available to pay this marital debt.

Practically speaking, the issue ought not exist. Where second spouses file a joint return they take full advantage of all the tax benefits of the marriage; yet, he or she has been a partner to the one who defaulted in an important obligation of the taxpayer, reimbursing welfare for the support of that person's child. Thus, it is our contention the second spouse brings to the counsel table unclean hands to try to argue for part of that refund.

If in fact that second spouse is an independent wage earner, all they have to do is reduce their withholding, and they avoid any direct impact of the setoff. Instead they are using it as a savings plan while the family lives off the funds that should have been used to pay for the family support. They have enjoyed the extra income resulting from the failure to meet this obligation.

If the second spouse does not wish to participate, then that second spouse should not file a joint return.

There has been litigation claiming lack of timely procedure to review setoffs; yet, State law in courts of equity, or an equitable procedures, have traditionally provided for an accounting. Failure to recognize this or be cognizant of it at the Federal level I submit has been a problem that should not have existed.

Thus, the program has had its problems in its implementation; but these mountains are, in may cases, molehills, if problems at all.

However, here is how, if I can run through them quickly for you, how I think we might improve the program:

The problem of declining proceeds in the future is being aggravated by the obligated parent being permitted to roll over his or her refund to meet the following year's taxes. Setoffs of funds owed the government ought to be given priority.

Kokoska and Enfinger, the two cases I cited, declaring that refunds are not tied to the underlying basis for the payment in in the first place, but that refund are debts that accrue only at the time a return is filed, could be reduced to statute.

The California community property law concept as to refunds ought to be adopted as Federal law, thus eliminating the problem of the joint tax return that has been referred to here previously.

Regional IRS centers ought to forward intercepted funds directly to State agencies in their region where both the debtor and the State agency are in the same region. That would cut out three or four separate pairs of hands on that money and reduce this delay so that errors could be corrected that much more quickly, at least where everybody resides in the same region.

Where the setoff is being expanded to cover unliquidated debts such as student loans, make it clear that such obligations are distinguishable from support obligations established by court or adminisrative order. Make clear the imposition of a support order satisfies any need for a preseizure or presetoff hearing. Be careful to avoid burdening the system with a plethora of preseizure hearings where the obligated parent already has had his or her day in court. Make clear the Federal Government does not consider itself bound by repayment agreements designed for the convenience of obligors and structured in the quasi-criminal context of contempt.

Sanction by statute acceleration of payment.

Should the setoff program be extended to other public debts, give priority to the support. Recognize that family support is one of the basic civil obligations of not just a citizen but any human being, and it ought to take priority over student loans or even taxes.

In bankruptcy cases, clear up the gray area that has occurred where the bankruptcy court declares that the setoff ought to be used to satisfy other debts, rather than to require the bankruptcy court to recognize this is a legitimate governmental setoff.

And finally, extend the program to seize refunds to pay support in nonwelfare cases. Use the concept of garnishment in such cases, and thus avoid any confusion with the governmental prior right of setoff, and also, almost by that simple use of language, enter into your Federal law all of the processes that are used to protect garnishees and provide for simple, quick, after-the-seizure hearings that are provided in most State courts.

IRS, in relation to the practical problem they have raised about costs, should recognize that they are, by keeping people off of aid, saving an enormous amount of money.

I have testified previously to this fact before the committee, but I will state it again: It costs four times as much to open an AFDC case in California as it does a child support case. Half of that money that it costs to run an AFDC case—even if you never spend a nickel; this is just administrative costs; even if you never pass out a grant—half of that cost is Federal money. IRS will be saving the

taxpayer an enormous sum if it can prevent or reduce the possibility of welfare dependence.

The tax refund intercept program has proven to be an effective revenue procedure for the Government. Problems have occurred; they are being ironed out. Legal issues have been raised—they are not insurmountable. Many can be resolved by legislation right here.

The public has awakened to the fact that it has been refunding large sums of money to individuals who have been absconding on the most basic of obligations to their family and society. At best, such a course of conduct makes the Federal Government appear foolish. The system has now been set in place to in part remedy this. Commonsense in terms of the cost of welfare as well as the sense of justice and fair play say this system ought to be extended to those who have suffered personally from family abandonment. The statute, 6305, is already, in a sense, in place to do this. All that is necessary is to simplify that statute. To not do so at this time, in the face of the census data statistics, in face of the collection statistics that we have, to deny single-parent families the simple effective way to remedy the wrong done to them in the fact of the evidence, is no longer to simply appear foolish, but it is to appear indifferent, unfair, or worse.

I thank the chairman and the subcommittee for permitting me to present these views.

[The prepared statement of Michael E. Barber follows:]

STATEMENT OF

MICHAEL E. BARBER
LEGISLATIVE REPRESENTATIVE
CALIFORNIA DISTRICT ATTORNEY'S
FAMILY SUPPORT COUNCIL

submitted on behalf of the

CALIFORNIA DISTRICT ATTORNEY'S ASSOCIATION

and the

CALIFORNIA DISTRICT ATTORNEY'S
FAMILY SUPPORT COUNCIL

to the

SUBCOMMITTEE ON OVERSIGHT OF THE
INTERNAL REVENUE SERVICE

COMMITTTEE ON FINANCE

concerning the Tax Refund Offset Program

September 16, 1983

Principal Parts of Testimony

I. The tax setoff program has been effective and should be continued. It has produced significant results in reducing the amount of child support owed the public.

II. Purported problems with the program may easily be resolved.

A. Reductions in withholding limiting recovery do not appear to have occurred. Such reductions as have occurred may be explained by other factors.

B. Administrative problems as have occurred could be remedied by adjustments in IRS procedures. It appears they already have to some degree this year.

C. Issues raised in litigation are not novel. They have been resolved at the state level in the context of family law. Thus, problems with characterizations of refunds, repayment agreements, second spouses and the like have been resolved.

III. Recommendations

A. Legislation be enacted to clarify:

1. The debt character of the refund distinguishing it from wages.
2. The obligation entered into by second spouses in filing a joint tax return.
3. The inability of local authorities or courts to waive the right to accelerate repayment of support.

B. Should setoff be extended to other obligations, the law should state:

1. The priority of support over these obligations.
2. The procedural finality of a hearing establishing a support order.

C. Non-welfare support should be enforced by seizure of refunds.

1. In any case where similar "choses-in-action" could be garnished;
2. Where there is an order for support payable through a IV-D agency; and
3. Adequate procedures exist for post-seizure review of the claimed default on the order.

This will both save tax dollars and reinforce our respect for the law.

Mr. Chairman, Members of the Subcommittee:

I want to thank the Subcommittee for the opportunity to submit this statement to you on behalf of the Family Support Council of the California District Attorney's Association. I am Michael E. Barber, Legislative Advocate of the Family Support Council. I am here on behalf of Edwina Peters, President of the Family Support Council, the Executive Committee of that organization, Donald Stahl, President of the California District Attorney's Association, and the California District Attorney's Association, to review with this Subcommittee the present tax refund offset program as it applies to past-due child support, and to recommend that the program be extended to collection of all child support without regard to the welfare status of the case.

The tax refund offset program went into effect at the federal level for the first time in 1982. It had previously been in effect at the state level in fifteen states for three or more years and had been a success at that level. It was a success at the state level and has been successful at the federal level; notwithstanding the criticism it has endured. I will attempt to respond to that criticism in this testimony and as stated above encourage that the program be expanded.

Briefly stated, the program involves set off against tax refund sums due the state and federal government as past-due child support (or child and spousal support) that should have been paid instead of Aid for Families with Dependent Children funds under Title IV-A of the Social Security Act. In the last two years under this program, the public has gotten back over $300,000,000 of the funds it has spent supporting defaulting parents' children. In California, the return has been in excess of $70,000,000. The program has, at least in California, resulted in a substantial reduction of the amounts past due in these cases. In the first year, California identified $549,000,000 as unpaid and past due. In the second year the cumulative total was $504,000,000. This was true even though there was greater participation by counties than during the first year.

There have been secondary benefits as well. First, we have been able nationwide to get an accurate accounting on sums due in these cases. In the first year, the total exceeded $1,760,000,000. In the second year, more jurisdictions participated and, as was the experience in California, participating jurisdictions submitted more cases. The result was a cumulative total of past-due support of almost $2,500,000,000. While this figure still understates the problem, we know now approximately how much non-support has cost the public, at least in cases where there was an enforceable order for support.

It has also resulted in obligated parents paying voluntarily support they had ignored. By bringing to their attention this sum due, we have all had scores of cases pay off their delinquent support. Neither they nor we wish to be entangled with the Internal Revenue Service. Notice that they are produces favorable results.

It has resulted in the location of delinquent parents. We are amazed at the number of parents who have been found to have good jobs yielding substantial income, even though parent locator services have not found them over the years. Now they have been found, much to their irritation.

It has resulted in correcting accounting data in our child support offices. By trying to enforce payment of support in this manner, cases have come to the fore where the custodial parent was taking the support directly and not reporting it. In some cases this conduct was through innocent error. But in others, it was the result of a deliberate effort to cheat the public out of the funds due the public.

But nothing effective ever seems to come without problems and the IRS intercept program falls within that precept. The problems fall within three categories.

First is a concern about continuing effectiveness. Second are program administration problems, and third are problems with litigation.

It is conceded that collections under this program have

diminished in the second year, at least as to California. If the trend continues, then in the long range it is conceivable the immediate cash return will diminsh greatly, if this trend is because of the change in withholding by the obligated parent. However, there are substantial reasons why this may not be the case. First, state experience with the concept does not support the proposition that people reduce their withholding because of a setoff, at least in the aggregate. During the several years this program was solely a state program in California collections actually increased. Thus, at least at the state level, withholding was not reduced because of a setoff.

At the federal level, this prior state experience is being duplicated. Notwithstanding the large amount collected last year ($168,000,000), collections this year are running ahead of last year ($169,000,000).

The California experience can be explained as a temporary phenomena resulting from the tax reduction, a slower economy, and the fact the first year cleaned up many vulnerable cases. As a consequence, it can fairly be said that the whole concept has proven its viability as a revenue raiser and justifiable relief for the taxpayer. Two years federal experience plus state experience justifies continuing and expanding the program.

But administration of the program could be improved. There have been problems in dealing with complaints and errors. Much

of the problem appears to lie at the federal level. First, there is the problem of inaccurate information being given the taxpayer by regional IRS offices and by federal notices. The federal notice would lead one to believe the funds have been transferred directly to the states. In fact, they are transferred to Washington from the regional offices by the Treasury, transferred from the Treasury to H.H.S., transferred from H.H.S. to the state governments, and finally back to the local agencies that correct the records. However, both the federal notice and the original information centers are leading people to believe that corrections may be made at the local level as soon as the individuals are notified by regional IRS of the setoff. This both irritates people and delays paying refunds where the funds have been set off in error.

IRS, according to state sources, is less than fully instructive to state government about the information they are giving regional personnel in this matter. If these were released to state governments, much confusion might be cured.

Delay in transfer of funds creates its own problems. While state tax authorities forward funds within four weeks, federal tax authorities have taken eight to ten weeks. Whether the funds are due the public and necessary to balance the books on a case, or are due the individual because of a correction the obligor has made or the public has made, this is too long a delay in transferring these funds. It would be a simple matter to transfer the funds

directly to states from regional centers, at least where the state designating the setoff and the obligor both reside in the same region. This could be done by Zip Code.

Setoff lists are required four months before the end of the year of setoff. Where errors have been made or delinquent sums paid off and deletions could be made from the setoff lists before setoff occurs, the federal government has not offered a timely process for doing so. Yet, at least in California, deletions may be made on our state tax lists right up to the date the check is forwarded to the county from the state. This inefficiency has caused considerable needless irritation.

The federal notice of setoff given the obligated parent has proven to be less accurate than similar state notices. Amounts are different from sums actually forwarded, states that have no interest in the case are being cited as the ones calling for the setoff, and setoff letters are being sent out with the refund check being sent to the taxpayer nonetheless. States and counties have set up revolving funds to pay refunds in advance of receipt of these funds from tax authorities where the names should have been deleted from the lists. When the matter is one involving state taxes, the state counterpart of the notice of setoff can be relied on and payment forwarded without a problem. But where the federal government is involved, actual transfer of funds to the state or local level must occur before a refund may be sent out.

Where there is an error at the federal level and funds have been in fact lost in the system, there seems to be no clear way to get funds forwarded to the individual. While this is a rare case, it would seem a complaint desk and a federal revolving fund ought to be set up to protect the obligated parent and to let the federal government correct its own errors.

Incorrect terminology and a lack of understanding of family law is the final problem. Thus IRS personnel were referring to second spouses in these cases in terms that would lead one to believe they were "wronged" or "injured". As will be discussed presently, this is an incorrect perception of the role of this individual in the process, but one that could result in significant public perception problems for this program. Terms such as "wronged" or "injured" have now been dropped from the vernacular, but not without public relations injury to the program.

In preparing for litigation, we have found federal attorneys, save and except those from the Office of Child Support Enforcement, to be unprepared to deal with issues that had long been resolved at the state level in family law context. Since federal judges often are also inexperienced in family law, issues have been given a degree of importance at the federal level that they do not warrant. Similar issues have been disposed of at the state level rather summarily.

The first of these issues is the characterization of the

refund. Certain forms of financial resources, specifically earnings, are given greater protection in law over others, such as stocks, bonds, savings accounts and the like, particularly where the funds involve support. The cases of Kokoska v. Belford (1974) 417 US 642, and Enfinger v. Enfinger (MD Ga 1978) 452 F Supp 553, have both conclusively established that the refunds are not treated in law as wages. They are analogous to a savings account and are a result of a complex mix of deductions and exemptions resulting from income from property, sale of property, and the like. Still and nonetheless, this issue continues to come up and may have resulted in at least one settlement adverse to the public in the State of Washington.

A second issue is the need for a hearing prior to seizure of the refunds. The uninformed on this issue overlook procedural protections already in the system for the obligated parent. First, since the set-off regulations require that it be based on an order of a court or administrative tribunal, there already has been a hearing. It has been held in California that no second hearing is necessary, the obligor has had his day in court when the order was entered, even if the sums seized are wages. Of course, a hearing after seizure must be available, and such a procedure is available in the form of an accounting. A second point often lost sight of is the importance of the funds vis-a-vis the needs of the family. As is pointed out by the Supreme Court in Kokoska above, these refunds are

a savings plan, within the control of the taxpayer. They are not by definition funds relied on for day-to-day sustenance. Thus the practical foundation for the prior hearing cases does not exist here.

Third, these intercepts are claimed to be unfair because in some cases there has been an agreement to reduce the delinquency through an orderly deduction from wages. It is claimed that there is a contractual waiver of the right to accelerate payment. What is lost sight of is that the consideration for a contract in such cases is, as to the public, illusory since the payoff rate often does not equal even the statutory interest that ought to have been paid on such sums. The public enters into such agreements for the convenience of the obligor and to meet minimimum standards of the courts in avoiding a contempt charge. The public loses on such arrangements because the repayment is interest-free and paid in inflated dollars. To allow the obligated parent who has already ripped off the public and violated the law by failing to pay support in a timely manner to further delay payment and pocketing a tax refund is unfai, but to the taxpayer. Yet we find federal officials and the Treasury in particular unaware of the basis of such repayment programs and unnecessarily troubled by them.

Fourth, we have the problem of second wives. Insofar as this is a problem, it should be noted this was repeatedly called to the attention of H.H.S. by state officials before the first year

of the program. They were advised to review state law and determine how other joint accounts were treated for garnishment procedures. Yet when the program went into effect, confusion on this issue reigned and state authorities had to do their homework independently. In California it was found that community property law made such funds totally available for support obligations. As a consequence, it became a non-issue here (absent a premarital agreement). Presumably this is the law in other community property states, yet in the Washington case referred to above, Treasury attorneys conceded half the refund was exempt from the intercept. Unless the Treasury misconstrued the refund to be wages of the second spouse, this result is inexplicable under California community property law. Washington is also a community property state. Legally then, the issue may not even exist.

Practically speaking, the issue ought not exist. Where the second spouse files a joint return, she (or he) takes full advantage of all the tax benefits of the marriage. Yet she (or he) has been a partner to one who has defaulted in an important obligation to the taxpayer -- reimbursing welfare for the support of that person's children. Thus the second spouse brings to the counsel table unclean hands. As a member of the family, the second spouse has enjoyed the extra income resulting from failure to meet this obligation. Why should that spouse not also be called upon to forego the benefit of government largess in the form

of benefits of a joint return. If the second spouse does not wish to participate, then that spouse should not file a joint return.

Finally, where the second spouse is a wage earner, that spouse could control the amount withheld. Thus, as a practical matter, sums are being kept from the second family that could have resulted in more liquid assets being available to meet current support, and saved with the Treasury, while the public is picking up the cost of raising the children. Now the second spouse is asking for the right to pocket these funds. Should this logic carry through, someone has indeed been wronged. It is the taxpayer. Yet as pointed out, at the federal level the second spouse was initially described in terms reserved for innocent victims.

Fifth, there has been litigation claiming lack of timely procedure to review such setoffs. I can only speak for California, but under our procedure where disputes about delinquencies cannot be resolved by negotiation, the filing of a motion for an accounting (a "Gabriel" motion) can quickly be put before a court and resolved. I cannot believe that other states do not have like or similar legal concepts. But because federal officials have not taken the time to understand family law practice, such concepts seem to have not found their way into federal cases with adverse consequences at the District Court level.

Thus the program has had its problems in its implementation. As is shown by the above, many of these mountains are in fact mole

hills, if problems at all. The press comment and litigation thereon and the program results have proven two things, however. First, as has been claimed repeatedly, the resources are there to meet support obligations. Secondly, obligated parents and their second families don't want to pay support, even when the result is to make the wronged taxpayer pick up the bill. They would rather pay attorneys to litigate.

While problems in administration such as outlined above should be dealt with, the various objections to the program that have come up in litigation would seem to warrant not a retreat therefrom but a forceful response from Congress. It is evident that collecting support through refunds is effective and fair. The program has worked and so should be both reinforced and extended. In this regard I wish to close with several recommendations.

First, the problem of declining proceeds in the future is being aggravated by permitting the obligated parent to roll his, or her, refund over to meet the following year's taxes. Setoffs of funds owed the government ought to be given priority over such rollovers. The taxpayer otherwise is stuck with a bill for the child that ought to be paid now.

Second, the Kokoska and Enfinger cases ought to be reduced to statute, making it clear that when funds are withheld or paid quarterly, they become federal property and become a debt to the person from whom withheld only when a return is filed and approved

or litigated.

Third, the California community property concept as to refunds ought to be adopted as federal law, at least where joint returns are filed. The unobligated spouse under California law is given a right of recovery from the assets of the obligated spouse for the community property used for support, should the second family ever dissolve. This too could be made a part of this statute. By adopting this property concept, the issue of the second spouse could be fairly and uniformly resolved nationwide.

Fourth, require regional IRS centers to forward intercepted funds directly to the state agencies in their region where both debtor and state agency are in the same region. Also require IRS to clarify the procedure in its notices and statements and advise state agencies of its procedures.

Fifth, where the concept of setoff is being expanded to cover unliquidated debts, such as student loans, make it clear that such obligations are distinguishable from support obligations established by court or administrative order. Make it clear that the imposition of such a support order satisfies any need for a pre-seizure or pre-setoff hearing. Be careful to avoid burdening the system with a plethora of pre-seizure hearings where the obligated parent already has had his or her day in court at the time the order was entered.

Sixth, make it clear that the federal government does not consider itself bound by repayment agreements designed for the

convenience of obligors and structured in the quasi-criminal context of contempt. Sanction by statute acceleration of such payments.

Seventh, should the setoff program be extended to other public debts, give priority to the support obligation. Recognize that family support is one of the basic civil obligations of not just a citizen but any human being and ought to take priority over student loans or even taxes.

Eighth, in bankruptcy cases, require that, where a setoff has occurred, the bankruptcy court recognize the setoff and permit the government to recoup its support debt therefrom.

Finally, extend the program to seize refunds to pay support obligations in non-welfare cases. It is already the law that such may be done (I.R.C. 6305), but the procedures are obtuse and cumbersome. The theory should not be setoff (since there are no mutual debts), but garnishment, but the need is as great. The statistics that demonstrate the direct correlation between AFDC dependence and non-support are redundant and overwhelming. Aside from the fact the present situation is unfair to non-welfare families and makes the federal government an aide and abetor in contempt of court and criminal non-support by the delinquent parent, the concept would be cost-effective as well. It costs four times as much to open an AFDC case as it does a child support case in California. The savings in administration in not having to open a welfare case,

aside from grant savings, would pay for the activity. Since any change in circumstances could result in AFDC dependence, by saving this money, the Internal Revenue Service would be saving tax dollars just as certainly as if it collected them itself from the absent parent to repay welfare costs. It would also restore faith in the system for the deprived parent.

There are concerns expressed about such an expansion. I hope to deal with them briefly. As is shown by the above, the present program has not significantly impacted withholding, expansion should not either. Problems of readjustment of tax liability at a later date seem illusory when it is realized that such adjustments, if involving a claim against the obligated parent, would mean no more than that the government had advanced support to his (or her) former spouse. It is not as if a person wrongfully entitled to the money had made off with it.

To further ensure that the obligated parent is not unfairly burdened, the claims should come only from the child support agency, be based on a support order of a court or administrative tribunal, and that there be provision under the law of the state that entered the order for review of the competing claims of the parents before the funds are disbursed. Where the order is found in a state other than that which submits the claim, then the state submitting the claim should be required to provide for litigation of the matter in a convenient forum, if necessary in the forum where the order was

entered. In other words, a case cannot be submitted unless the submitting agency is prepared to have the claim properly reviewed.

Billions of dollars in unpaid child support are accruing nationwide. Families too proud to go on welfare are being victimized by this criminal conduct just as surely as is the taxpayer when the family goes on welfare. To simplify present law to permit those families' rights to be protected is no more than simple justice. When the high economic cost of welfare, a state to which even the proudest of these families may be consigned, is also realized, it is also economic common sense. It is hoped this right to garnish these refunds will be enacted speedily to permit implementation by January 1, 1984.

Summary

The tax refund intercept program has proven to be an effective revenue procedure for the government. Problems have occurred at the federal level because of administrative shortcomings that are now being ironed out. While there is some suggestion that the program may not produce as much revenue in the future as it has in the past, this problem still appears to be a mere shadow and may be explained by our economic malaise. More immediately it is reaching the group at which it is aimed and is inducing voluntary compliance with the law, even in cases where even coercion has failed in the past.

Legal issues have been raised but these are not insurmountable.

Some are illusory. Others may be resolved by legislation. Extension of the program is certainly warranted to other forms of debts to the government. But in doing so, the debt for support should be given the priority that any civilized individual ought to give it.

Finally, the public has at last awakened to the fact it has been refunding large sums to individuals who have been absconding on the most basic of obligations to their families and society. At best, such a course of conduct made the federal government appear foolish. A system has now been set in place to remedy this. Common sense in terms of the cost of welfare, as well as a sense of justice and fair play, says this system ought to be extended to those who have suffered personally from family abandonment. A statute is already in place to do so. All that is necessary is to simplify that statute for this purpose. To not do so at this time, to deny single-parent families this simple, effective way to remedy the wrong done them, in the face of the evidence, is no longer to simply appear foolish but is to appear indifferent or unfair, or worse.

It is respectfully requested on behalf of the California District Attorney's Family Support Council that the program to seize federal tax refunds be extended to all cases where child support payments are delinquent as speedily as possible.

I thank the Chairman and the Subcommittee for permitting me to present these views.

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Senator GRASSLEY. One of the things I was going to ask, and you went into considerable detail on it, is what sort of suggestions you have for improving our current system based upon California's experience, and you had a long list of those things. So I assume that you included all you felt ought to be in there.

Mr. BARBER. Yes, sir. I wasn't able to touch on them all, but I understand the time limit.

Senator GRASSLEY. Well, if you want to add to any of that in written testimony, we could have that.

Mr. BARBER. Senator, I certainly will.

Senator GRASSLEY. OK. Because our staffs ought to go down your list to see how we can benefit from that, as far as our legislation is concerned.

I think you have covered the point about how constitutional due process can be maintained. Is there any suggestion in your testimony that in our proposed legislation we have gone beyond what we needed to, to meet the constitutional due process?

Mr. BARBER. I haven't reviewed it to see whether or not you have required any subsequent hearings after the initial court order that establishes support. But it would be our position, given the fact that in fact we are giving people notice as soon as the notification is sent to IRS, that they may be intercepted, and they had better clean up the record. To me, that is more than ample notice, and in fact may defeat part of the program. They can then come into the office that sends them the notice and then clear up the problem; if in fact the problem can be created, it can be cleared up.

I think that, as a practical matter, if we could get the money back from IRS a whole lot faster, we would provide a better practical protection to people who have been wrongfully intercepted than any procedural rights that might be written into a statute. The biggest single practical problem is just getting the dough out.

We have established a revolving fund in our office, so if we found we had errors—and we have had errors in 5 to 10 percent of our cases in any given year. I will withdraw the word "error." Let's say we have had "discrepancies," because people have come in and paid off, or we have found that there were direct payments and fradulently received direct payments, and situations like that. But we found we had to make corrections in 5 to 10 percent of the cases.

With a revolving fund of a relatively small sum, established at the county level—$30,000 to cover our State tax refund program—we were able to make payoffs quickly, because the State in turn got that money out to us quickly.

But the Federal situation has been 8, 10, and 12 weeks before we saw the money, after the notice went out; it has been disastrous.

Also, the Federal notices are disastrous in terms of PR. Also the Federal notices about what is being intercepted and being forwarded have proven to be inaccurate in all to many cases. In State cases we can make State refunds based on State notices. Federal notices we can't rely on. We have to see the lists that actually come down from the Federal Government before we can make the refund. They have even sent money to the individual immediately after they have told him that his taxes were going to be intercepted and he wasn't going to get it. We have had those situations at the Federal level.

Senator GRASSLEY. I guess what we need further explanation on is from your testimony, where you say "a hearing after seizure must be made available."

Mr. BARBER. That's correct.

Senator GRASSLEY. We don't—I don't understand why a hearing after seizure as opposed to before.

Mr. BARBER. If in fact, for one reason or another, they don't have to take advantage of that hearing, and indeed they may have to kick in the cost; but that is a standard. So long as you don't have a hearing before, you are required in effect by law, by case law, to give them a hearing, a timely hearing, after seizure.

Senator GRASSLEY. OK. But if you have an opportunity for that beforehand——

Mr. BARBER. Then you would not need one afterward. I would prefer the after-the-fact hearing than the one before, based on the way our courts work and the fact that, for the most part, individuals are more likely before the hearing, even if they owe the money, to ask for it than they are after, and after he receives it, that only people who truly feel they can't work it out in the office are going to ask for it.

I might add, I worked on a State statute to handle a similar problem. We have required those people in the State statute to contact our office first, and if they don't contact our office within 15 days after the notice, they are foreclosed from getting that after-the-fact hearing. You might consider that in your statute, to cut down the number of spurious after-the-fact hearings.

Senator GRASSLEY. In your off-the-cuff remarks before you started your prepared statement, you requested that we not be overly concerned about the adverse impact on tax compliance out of respect for the honest taxpayers who do pay.

Mr. BARBER. Yes, sir.

Senator GRASSLEY. Do you have any feeling, though, whether or not it would have, just in and of itself, the tax offset principle, have any adverse effects on tax compliance?

Mr. BARBER. My gut feeling is that it would have just the opposite. There is a feeling out there right now that too many people are taking advantage of the system, and the individual who is paying fairly and forthrightly increasingly is becoming distressed. I end up on TV shows and on radio occasionally in Sacramento. People come up to me that I never saw before telling me what a great job we are doing and how we ought to go and get these individuals even more.

Senator GRASSLEY. My last question is narrower in scope and I raised it with other witnesses, is any evidence, in your case specifically, California, that high-income taxpayers might underwithhold for the purpose of avoiding tax offsets?

Mr. BARBER. No; there is nothing in terms of underwithholding in that regard. I think second spouses who are wage earners may well underwithhold to avoid being involved in it. I think there is going to be that aspect to it, but I think that's a relatively small group of people. That is their right within the tax system, if they wish to reduce the obligation. But I think the point that we could make, then, as prosecutors in these cases, is that then there is that

much more cashflow into the home, and the individual ought to pay the support through some other means.

Senator GRASSLEY. Thank you very much.

Mr. BARBER. Thank you, Senator.

Senator GRASSLEY. We appreciate your expertise in this area.

Our last witness is Willis Wolff, who is executive director of the Iowa College Aid Commission, and that's our State agency in my State for student assistance through scholarships, grants, and loans.

She began working for the commission in 1965 and has been its executive director for the past 7 years.

I have known Willis since I was a member of the legislature, and know her to be a person who is devoted to doing a good job.

Would you proceed?

STATEMENT OF WILLIS A. WOLFF, EXECUTIVE DIRECTOR, IOWA COLLEGE AID COMMISSION, DES MOINES, IOWA

Ms. WOLFF. Thank you, Chairman Grassley.

I really appreciate being invited to come and talk with you today and tell you a little bit about our Iowa program, and give you our reaction to the bill that is under consideration this morning.

As Iowa's State agency for student aid, we administer scholarships and grants as well as the student loans and the parent loans, the PLUS loans. However, the guaranteed student loans and PLUS loans are generating five times the private capital as the amount of State funds that we have in State scholarships and grants. We have $20 million, approximately, in the grants, and we are generating about $100 million in private capital for the loans every year.

Together, these programs are helping better than one out of every two Iowa students.

Just a little background on our program: From the inception of the program 4 years ago, our commission was determined to keep it a community-based program. It was our goal to get just as much participation in that program as we possibly could.

As you know, Iowa has a great many lending institutions. We have virtually every bank, savings and loan, and credit union in the State, a total of about 670 lending institutions, involved in making loans to Iowa students right now.

Over the past 4 years they have invested $400 million in loans to students, and $3.5 million over the past year in loans to parents under the new Iowa PLUS program that just started a year ago last May.

Now, these are all positive comments that I've made so far; but I don't have to tell anybody that the guaranteed student loan program has lots and lots of problems. And very high on the list of those problems are defaults. Actually, in Iowa we don't have too much to complain about yet, because our default record is quite good compared to the national averages and the averages you find in other parts of the country. But since the inception of the program we have paid out $4.5 million in default claims. That does not include death and disability and bankruptcy.

Based on the $102 million in loans that have entered into repayment so far, that's a 4.5-percent default rate. It's not too high com-

paratively speaking. The national comparable default rate would be about 15 percent, I believe, if you include the federally insured paper as well as the guarantee agency paper.

Our collections? I'm sorry to say I'm not proud of our collections at this point. They amount to $123,000 on the defaults that we have had. This is just about, not quite but almost, 3 percent of the defaults. That's not good enough in the view of our Commision, and we're taking steps to improve that.

Now, you understand we are just reaching the point of maturity in our program and beginning to realize a full quota of defaults. So we are doing a number of things, and one of the things that our State has done in the last year is to establish the State tax refund offset for guaranteed loans. It has been in effect for child support payments for about 3 years in Iowa. And the legislature, upon the recommendation of our agency and with the Governor's support, has extended this provision to student loans.

The recoveries so far have not been very impressive, because we just began claiming tax refunds this past year. We have collected $10,000. We have had 23 matches between the default and tax refund records. Some of those matches were for students who were already into repayment, so we did not preempt their refunds since we have them on a steady repayment mode, we saw no reason to go in and take their refunds.

I think that the psychological impact of this tax refund offset has been important in convincing possible potential defaulters that Iowa really means business in collecting student loans. And we do, indeed.

We are adding a collection unit to our staff; we also are working currently with four collection agencies. And, incidentally, you might be interested in our rates. We are paying from 20 to 25 percent to these agencies. We want to do as much collection inhouse as we can because we get better results that way.

Now, Senator Jepsen's bill, Senate 150, is proposing that the IRS be empowered to give the State agencies and the Department of Education assistance in collecting student loans. We are all for that. We can certainly use all the help we can get in collecting defaults.

Going after student loans in the same way that the IRS goes after delinquent taxes, I think, might be a very effective measure in convincing willful defaulters that they just "better not do it," that they are going to be caught up with sooner or later.

I believe that there are a lot of technical details, as Mr. Elmendorf pointed out, that would need to be resolved in that program. There would have to be a high degree of coordination among the collection efforts of the State agencies, the Department of Education, and the Internal Revenue Department. I do believe those technicalities could be ironed out and that it would be an effective deterrent and collection tool

Of course, Ed Elmendorf also pointed out that prevention is just as important as cure, perhaps more so, in keeping defaults down. This is certainly true. And we think in Iowa that the one-on-one relationship between the lender and the student borrower is very valuable. We encourage our lenders to ask for cosigners if they want to; many of them do, particularly the small banks and sav-

ings and loans. We encourage the lender whenever possible to interview the student and convince that student that this is not a gift, that it is going to have to be repaid, that he has an obligation.

We have not, like many States, turned to a big central lender or to tax-exempt bonding in order to fund student loans. We have relied on the great number of lending institutions in our State and have utilized them, and they have cooperated with us wonderfully.

Now, we don't impose any unnecessary restrictions, but we do expect these lenders to treat student loans just as they would any other obligation, any other consumer loan, and practice due diligence in trying to collect those loans.

We believe that every student is entitled to loan access if that student needs it, and we do have last-resort lenders in Iowa. We have larger lenders that will make a loan to any qualified student under our agency's guarantee. So they do have full access.

We also think every student is entitled to access to good counseling, counseling against borrowing when it is not necessary, counseling against the pitfalls and the dangers of extending their indebtedness too much, more than they can repay. And we do believe, also, that these entitlements can best be carried out under the auspices of a single State-controlled. State-appointed agency, which is answerable to the State legislature and the State comptroller. We think that was the intent of the higher education amendments, and we hope that Congress will keep it that way.

We do thank you very much for letting us give testimony.

Senator GRASSLEY. Thank you.

[Ms. Wolff's prepared statement follows:]

TESTIMONY

BEFORE THE SENATE SUBCOMMITTEE

ON

OVERSIGHT OF THE INTERNAL REVENUE SERVICE

September 16, 1983

BY: Willis Ann Wolff
Executive Director
Iowa College Aid Commission
201 Jewett Building
Des Moines, Iowa 50309

Summary of Testimony
by
Willis Ann Wolff, Executive Director
Iowa College Aid Commission

Guaranteed Student Loans and PLUS Loans are possible through a 4-way partnership benefiting students, lenders, schools, local communities, and the Nation.

Grassroots involvement is the key to success of Iowa guaranteed loan programs

* More than 670 lending institutions participate

* $400 million in Iowa Guaranteed Loans over past 4 years

* $3.5 million in Iowa PLUS loans since program began in June 1982

* 50% of Iowa college students have Iowa Guaranteed Student Loans

Default recoveries are a major problem for guarantee agencies

* Iowa defaults low compared to national averages - $4.5 million or 4.5% of matured paper

* Collections to date - $123,000 or 2% of defaults

* Steps being taken to improve collections include new state tax setoff, added collection staff for Commission, use of four outside collection agencies, skip tracing with help of Internal Revenue Service

Senate Bill 150, sponsored by Senator Roger Jepsen, would give Internal Revenue Service a partnership role in collection of defaulted loans

* State agencies welcome this assistance

* Close coordination between state guarantors, Department of Education and Internal Revenue Service will be essential

* Will be psychological deterrent to willful defaulters, as well as collection tool for the $300 million in claims being paid annually

Default prevention equally as important as cure

* Students are entitled to full loan information and access to necessary borrowing, with adequate counseling against over indebtedness

* Best insurance against misuse and abuse of education loan --

  - One-on-one relationship between lender and borrower, whenever possible

  - Decentralized administration on a state-by-state basis through a single state guarantee agency authorized by appropriate state entities and the Department of Education

Chairman Grassley, Members of the Committee:

I appreciate the opportunity to appear before you today as a representative of the Iowa College Aid Commission, the agency responsible for administration of state scholarships, grants and loans for college students in Iowa. Specifically, I have been invited to bring you information about the Iowa Guaranteed Student Loan Program and the Iowa PLUS Loan Program, which currently are providing aid to one out of every two Iowa postsecondary students.

Our Commission views the Guaranteed Loan and PLUS Programs as a four-way partnership which benefits everybody involved. The students and their parents benefit directly from the loans, which make it possible for many to realize their educational goals or help their children to get college degrees.

The State and Federal Governments benefit through the long-range product of broad educational opportunity -- a well-prepared citizenry capable of becoming our business, professional, technological and political leaders of tomorrow.

The lending institutions benefit through using their private capital to make guaranteed loans at a profitable interest rate and, at the same time, serving the citizens of their communities in a tangible way.

The communities themselves benefit -- not just the college communities that depend on students for a healthy economy -- but all communities in need of well-educated citizens for their future survival.

This philosophy of a grassroots partnership with many contributors and beneficiaries has been the touchstone of the success of Iowa's loan programs. Practically every bank, savings and loan association and credit union in our state -- more than 670 in all -- is making loans to Iowa

college students and their parents. Very few lenders were participating in the earlier federal student loan program, and students found it difficult to get loans. Iowa students have no loan access problems now. Over the past four years, Iowa lending institutions have invested more than $400,000,000 in loans to Iowa students. The PLUS Program has been in operation only a little over a year in our state, but during that year more than $3,500,000 has been loaned to parents to help them budget the cost of educating their children, to graduate students and to self-supporting undergraduates.

Everything I have said so far has been on the positive side. But the guaranteed loan programs present plenty of problems, as I know it's unnecessary to point out to this Committee. Close to the top of this list of problems are defaults. It has become fairly easy for any qualified student to get a loan, thanks to the close-to-the-source promotion and development of these programs by state agencies. Paying back the loans is often far more difficult.

Our defaults in Iowa really are not alarming yet, compared to nationwide averages. Since May 1979, when the Iowa program went into operation, our Commission has paid default claims totaling $4,581,637, death and disability claims totaling $458,309, and $348,219 in bankruptcies. With $102,000,000 in loans that have reached repayment, our default rate comes to 4.5 percent.

We have collected $123,000, slightly less than 3 percent of those defaults. This is not nearly good enough, in our opinion, and we are taking a number of steps to improve our collection record.

Upon our Commission's recommendation and with the support of our Governor, the State Legislature has authorized the Revenue Department to withhold any tax refunds for people who are in default on their Iowa

Guaranteed Student Loans. These refunds are turned over to the Iowa College Aid Commission to be applied toward repayment of the loans. Of course, 70 percent of this money goes back to the Department of Education, as do any other recoveries that we realize on defaulted loans. The new tax refund offset has been in effect for less than a year, and we feel it is going very well. We have collected about $10,000 in tax refunds, and there have been a number that we did not preempt because the loan already was being repaid at a satisfactory rate. Perhaps equally as important as the recoveries from tax refunds is the impact of this measure in convincing the public that the State of Iowa really means business on loan collections.

We are adding a collections unit to our Guaranteed Loan Division, and we expect to handle an increasing amount of this work ourselves in the future. At present, we are using four different collection agencies to assist our staff in tracking down defaulters and getting them into repayment. It's a challenging job, and we need all the help we can get.

The guarantee agencies already are receiving assistance from the Internal Revenue Service in skip-tracing defaulters. Updated address information is being provided on a regular basis at the request of the guarantee agencies. We welcome Senator Roger Jepsen's proposal that the Internal Revenue Department cooperate with the Department of Education and the state agencies in collecting defaulted student loans. Going after student loans in the same way that the IRS goes after delinquent taxes -- and applying the same penalties -- might go a long way toward dramatizing the obligation to repay these loans. With close coordination among the state and federal agencies concerned, I believe that Senator Jepsen's Senate Bill 150 would bring solid results in reducing the more than

$300,000,000 in reinsurance claims that the Federal government has been paying annually.

Of course, prevention is equally as important as cure in keeping defaults at a minimum. The Iowa program was built on a foundation of hometown lending institutions, and we are doing our best to keep the loans close to the community. The loan least likely to default, in our experience, is the transaction between a borrower and a local lender who may have done business together in the past and who plan to continue doing business in the future. Approximately 50 percent of the Iowa student loans have been made by lenders with student loan portfolios of less than $1,000,000. The default rate on these loans is negligible.

Of course, not every student who needs to borrow is fortunate enough to have a friendly lender to turn to for student loans. Iowa is blessed with a rich variety of financial institutions, and there are any number of lenders who are willing to make loans to such students under our Commission's guarantee.

The Iowa program imposes no unnecessary restrictions on student loans, but we do ask the lenders to handle these loans in the same businesslike way that they would apply to any other consumer loan. We encourage, but do not mandate, co-signers and preliminary interviews with the borrower. We do require that the loan check be sent to the borrower's college for delivery after the school term begins.

We believe that every eligible student is entitled to full information and access to all forms of college aid, including guaranteed loans. We also believe that every student is entitled to adequate counseling against unnecessary borrowing and the pitfalls of over-indebtedness.

Our Commission believes that these student entitlements can best be served by a single officially designated guarantee agency in each state working in partnership with the lenders, the schools and the Federal government. We believe that this was the intent of Congress as embodied in the Education Amendments of 1976 which persuaded Iowa and many other states to enter the guaranteed loan program.

If Congress and the Department of Education wish to build upon the success achieved by the state guarantee programs, all possible measures should be taken to protect the decentralization of the loan programs on a state-by-state basis. The best insurance against misuse of these excellent and much needed programs is to preserve the original concept of one designated guarantee agency per state, operating under the official surveillance appropriate for tax-supported programs.

Thank you for permitting me to testify before this Committee.

Ms. WOLFF. Can I answer any questions for you?

Senator GRASSLEY. Yes, I think so. Some of them you have answered. You have stated what your current default rates are.

Ms. WOLFF. Yes. It's 4.5 percent, based on loans and repayment.

Senator GRASSLEY. And I assume that your support of S. 150 would indicate a feeling on your part that that was significantly correct, that default rate?

Ms. WOLFF. I think it would certainly prevent it from going any higher. You know, with a program of unsecured loans you are going to have a default rate. If we can keep that default rate under 5 percent, I think we would be doing well.

Senator GRASSLEY. Do you have a perception that IRS would aggressively collect delinquent accounts if referred to them? And I guess I would ask you to think in terms of that IRS, like maybe any other Government agency, feels like they don't get adequate appropriations to do the job that they have mandated to them.

Ms. WOLFF. That is probably true. It would have to be a partnership effort, I think, between the Department of Education, IRS, and State agencies.

Senator GRASSLEY. I think that's all the questions I have. Thank you very much.

Ms. WOLFF. Thank you, Senator Grassley.

Senator GRASSLEY. I'll see you next week before another committee.

Ms. WOLFF. Fine.

Senator GRASSLEY. The hearing is adjourned.

[Whereupon, at 12:35 p.m., the hearing was concluded.]

[By direction of the Chairman the following communication was made a part of the hearing record:]

NORTH CAROLINA
STATE EDUCATION ASSISTANCE AUTHORITY
GENERAL ADMINISTRATION: THE UNIVERSITY OF NORTH CAROLINA
UNC RESEARCH TRIANGLE PARK BUILDING, ALEXANDER DRIVE
RESEARCH TRIANGLE PARK
(919) 549-8614

Stan C. Broadway, *Executive Director*
Charles F. George, Jr., *Associate Director*

Mail Address:
Box 2688
Chapel Hill, N.C. 27514

September 26, 1983

Senator Charles Grassley
135 Hart Senate Office Building
Washington, D.C. 20510

Dear Senator Grassley:

As an agency of State government charged with the responsibility for making student educational loan credit available and for collecting student loans, I write to support the principle set forth in Senate Bill 150. This bill, I understand, will require the Federal Government to demand the repayment of uncollected student loans through an offset against any Federal tax refund which may be due the defaulter. From our experience in the State of North Carolina, this is an important piece of legislation that should be enacted by the Congress as soon as possible.

Several states, including North Carolina, have enacted similar measures at the level of State taxation to recover defaulted student loans. The North Carolina General Assembly passed legislation several years ago which requires State agencies to submit to the North Carolina Department of Revenue a list of all persons with outstanding debts owed the agency. Checking this list of defaulters against the roster of persons scheduled to receive State tax refunds is accomplished through a computer match. Since 1980, we have identified more than 1,745 borrowers who owed this agency more than $257,000 through this debt offset process. Initially, the Department of Revenue was not enthusiastic about the prospect of becoming involved in debt collection. However, by exercising full cooperation among the agencies and by streamlining the process through computerization, the program has not proven to be a burden on the Department of Revenue. Indeed, it has worked to strengthen the collection effort of the agency which has paid out taxpayer funds to pay off the defaulter's rightful obligation.

The primary advantages of a debt offset act are: 1) an effective means of locating the borrower at little additional cost to the agency, 2) a strong enforcement arm beyond the mere voluntary effort of a person who made pledges to repay a student loan but who often break such promises, 3) a particularly strong psychological signal to defaulters and potential defaulters that the government is indeed serious about collecting the just debts owed to it, and 4) an especially cost-effective technique for debt recovery.

We believe that the enactment of the debt setoff act in North Carolina along with a companion act which requires State employees owing on defaulted student loans to make satisfactory repayment arrangements as a condition of continuing employment or obtaining employment initially with the State are the most effective steps that the General Assembly has taken recently to assure recovery of funds owed to the State.

Of course, such efforts are of little value when our defaulter does not reside in the State of North Carolina nor pay State income taxes. However, most would be living within the United States and paying United States income taxes. The efforts of the States to collect through a debt setoff act are limited and not completely effective unless the United States Congress enacts similar legislation with respect to Federal taxes. In our opinion, the objections which have been raised by the Department of Education, the U.S. Treasury and the Internal Revenue Service are without merit. There is ample evidence among the States that a debt setoff act can work effectively to restore funds to the Treasury which are justly owed to the Government.

Rather than complaining about the rising level of student loan defaults, we believe the Federal government should be enacting measures which strengthen the hand of those charged with the responsibility for collecting overdue debts. We urge prompt Congressional action on this measure.

Very truly yours,

Stan C. Broadway

Stan C. Broadway

SCB:np

cc: Senator Jesse Helms
Senator John East
Representative Ike Andrews

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