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STATEMENT OF
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BEFORE THE
HOUSE BUDGET COMMITTEE
ON



IMPROVING THE COLLECTION OF DEBTS
OWED THE GOVERNMENT

Mr. Chairman and Members of the Committee:

We are here at your request to discuss ways in which Federal agencies can improve their collection of debts owed the Government. We appreciate your interest and concern and greatly appreciate your support of our effort in this area.

Debts arise from a host of Federal activities, including tax assessments, sales of Government services and goods, overpayments to veterans and annuitants, and various loan programs such as student and housing loans. Most of these debts are paid routinely. However, some are not and amounts owed and being written off as uncollectible are substantial and growing rapidly.

At the start of fiscal 1982, Federal agencies reported that receivables from U.S. citizens and organizations exceeded

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\$180 billion--a 45 percent increase in the last 2 years. As of September 30, 1979, Federal agencies reported that about \$24 billion due from U.S. citizens and organizations was delinquent. By September 30, 1981, this delinquent amount had grown to about \$33 billion. Of this amount, approximately \$20 billion represented delinquent taxes. In addition, another \$8 billion in loans are in a rescheduled status because of the borrower's inability to repay their loan in accordance with the original terms specified in the loan agreement. Further, over \$1 billion in uncollectible receivables are being written off each year and it is estimated that an additional \$8 billion will be written off as uncollectible over the next several years.

As we reported last year, before the Government's debt collection problems can be remedied, many actions--administrative and legislative--must be taken. In general, there are two basic reasons why debt collection in the Federal Government has not kept pace with the increasing number of debts. First, debt collection has generally been afforded low priority with emphasis on disbursing funds rather than collecting them. Second, present Government collection methods are expensive, slow, and ineffective when compared with commercial practices. We have identified specific weaknesses in the Federal agencies debt collection programs and have recommended a number of specific corrective actions to improve the recording and collecting of debts owed to the Government. Our recommendations, unfortunately, have not always been implemented. Unless Federal agencies are provided with essential

collection tools and resources and until they aggressively pursue the collection of debts, hundreds of millions of dollars will continue to be needlessly lost.

ADMINISTRATIVE AND LEGISLATIVE ACTIONS
NEEDED TO IMPROVE DEBT COLLECTIONS

We have testified in support of comprehensive debt collection legislation presently before Congress which would give agencies many of the tools they need. Passage of S. 1249 and accompanying House bills would remove many of the obstacles that now preclude agencies from using collection tools that are widely used in the private sector. I would like to briefly mention some of the administrative and legislative actions we believe are needed.

Making debt collection an important
responsibility of management

Debt collection has generally been afforded low priority with the emphasis on disbursing funds rather than collecting them. In many cases, debt collection has been an afterthought with only limited personnel involved. Adequate resources have often been lacking in the past. Tools such as adequate accounting, billing, and collection systems that work and provide management the information needed to protect the Government's financial interest are essential. Top agency officials must take the lead if debt collection is to receive the priority it needs.

In this regard, in January 1981, the Office of Management and Budget released the "Debt Collection Project--Report on Strengthening Federal Credit Management." The report, based on the review and analysis of 24 Federal agencies and departments' debt collection

systems, made numerous recommendations to improve debt collection in the Federal Government. Further, the President, in a memorandum dated April 23, 1981, directed the heads of Executive Branch agencies and departments to develop and implement an aggressive debt collection program by:

- Designating an official with responsibility and authority for debt collection and submitting the name of the official to OMB. Twenty-four major departments and agencies have designated this official.
- Preparing a detailed review of current debt issues and outlining the action to be taken to resolve the issues and a timetable for completion of the action.
- Submitting an annual progress report on the results of the review to the OMB Director.

OMB's Council on Integrity and Efficiency has given high priority and dedicated full-time staff to strengthening Federal debt collection.

Charging interest on delinquent debts

Charging of interest is already required by Federal regulations as a payment incentive; however, many major agencies have not been complying. Further, in some major programs, such as student loans, the rates prescribed by law or set administratively are far below the Treasury's borrowing cost and commercial interest rates. Because these favorable interest rates generally continue even after the debt becomes delinquent, the debtor has a disincentive to pay the Government. We believe that unless there is a specific prohibition in the law, agencies should include in their loan

agreements a provision allowing for the rate of interest to be increased to the prescribed Treasury rate if delinquency occurs. This would provide an incentive to Government debtors to keep their payment current.

Reporting debts to credit bureaus

Commercial firms report loans incurred, credit card and charge account information, and installment payments to a credit network made up of a consortium of credit bureaus throughout the country. This practice is done to encourage debtors to pay off their loans and charge account debts in a timely manner or face the consequence of having their credit rating adversely affected. If Federal agencies could likewise report debts owed the Government, especially defaulted loans and delinquent accounts and loans receivable, to the credit bureau network, debtors would be more likely to pay their debts to the Government to avoid receiving poor credit ratings which would affect their ability to obtain future credit. This tool would be especially useful in the Government's efforts to collect debts for which, due to their small size, it is not practical to take legal action. However, legislation is needed to remove the obstacles that now preclude agencies from reporting to credit bureaus.

Contracting with private collection firms

One way the Government can reduce the amount of its uncollected debts, especially those too small for legal action, is through the use of private collection firms. This would be consistent with the commercial practice of referring debts to private collectors before considering them totally uncollectible.

A change to the Federal Claims Collection Standards, in April 1981, encourages Federal agencies to contract with private collection agencies, where appropriate, to supplement existing collection programs. Contracts with private collection firms have been awarded by the Department of Education and the National Credit Union Administration and are being studied by several other agencies. Continued emphasis on using collection firms is necessary especially in light of over \$1 billion in uncollectible receivables being written off annually. Federal agencies must use every means available in order to reduce the amount of delinquent debts owed the Government.

In February 1982, we sponsored a joint Government-industry debt collection conference to exchange ideas on how the private sector and Federal agencies can work together to collect debts owed the Government.

Removing restrictions on the redisclosure of addresses obtained from IRS

Locator assistance available from IRS is far more effective and less costly than any alternative locator technique. The usefulness of the IRS address information has been greatly restricted, however, because the Tax Reform Act precludes redisclosure of an address obtained from IRS to credit bureaus or other contractors who are assisting in the collection effort. Legislation is needed to remove this obstacle. S. 1249 and accompanying House bills, as written would permit redisclosure of IRS addresses to contractors assisting in the collection effort, but would prohibit redisclosure of the addresses by the contractor.

Consequently, use of credit bureaus to affect credit standings of the debtors would still be precluded whenever the debtor has been located through IRS.

Using the credit bureau debtor locator service

Another locator service available but seldom used is that provided by the credit bureau network. Agencies have accumulated a large backlog of delinquent debts and have written off hundreds of millions of dollars in debts because they could not locate debtors. Because millions of Americans have credit records, the service, which is inexpensive, can be a good source that is readily available. It has proven useful for commercial firms.

Collecting by offset

Another way of collecting many delinquent debts is for the Government to reduce or withhold future payments or benefits from the debtor. In practice, due to legal constraints or agency policy, offset has been used only in certain circumstances such as offset from (1) continuing entitlements to the same beneficiaries originally overpaid, (2) civil service retirement annuities or contributions, (3) final pay of Federal employees, (4) amounts due indebted contractors of the United States, and (5) judgments against the United States. Let us mention some other types of offset that should be considered.

--Offset of salaries of Federal employees. Under present legislation, the salary of a Federal employee may not be withheld to satisfy general debts owed the Government. An employee's salary may be withheld only to satisfy an

erroneous payment the agency made to the employee, or for travel or moving expense advances paid to the employee. However, agencies such as the Department of Education and the Veterans Administration have found that millions of dollars of delinquent debts are owed by Federal employees and could be collected by salary offset.

--Offset of Federal tax returns. GAO has long supported the use of tax refunds as a means of collecting outstanding amounts owed the Government. In our report titled "The Government Can Collect Many Delinquent Debts By Keeping Federal Tax Refunds As Offset" (FGMSD-79-19, March 9, 1979), we recommended that, on a test basis, agencies refer to the IRS for offset those debts which the agencies have been unable to collect through normal collection procedures. The IRS was unable to test the offset program because the Congress did not appropriate funds for the test. Subsequently, we reviewed the State of Oregon's offset program for collecting delinquent debts, which is similar to the Federal offset program we recommended. The Oregon program has proven most effective with collections through offset of \$3.7 million in 1980 at a cost of only \$220,000.

Clarify the 6 year statute of limitations

Because many debts are now or will be 6 years old before offset becomes possible, we have recommended that the statute of limitations be amended to explicitly recognize that the 6 year limitation does not prohibit the offset of debts owed the Government.

FEDERAL AGENCIES POLICIES AND PROCEDURES
FOR EXTENDING CREDIT NEED IMPROVEMENT

Collectability of debt is directly impacted by the initial policies, standards, and procedures for extending the credit. The OMB Debt Collection Project as well as our own reviews of Federal agencies debt collection programs found that the lack of strong and effective standards and procedures for screening and approving credit not only contributed to delinquencies and defaults, but also hindered collection efforts.

Most Government programs are intended to fulfill a social need and, as such, provide for more lenient and flexible standards than private sector credit functions. Frequently in these programs, the Federal Government is the lender of "last resort", making credit available to individuals and organizations that cannot obtain credit in the private sector. As such, private sector credit standards cannot be rigidly applied and still meet the social objectives of the programs.

However, Federal agencies can do more to protect the Government in extending credit to minimize potential debt collection losses. Some deficiencies and problems concerning the credit extension process are incomplete loan agreements, lack of procedures to share information on credit worthiness and inadequate management of collateral.

Incomplete loan agreements

The content of loan applications and agreements is often insufficient for credit management and debt collection purposes. Some agencies do not include "default clauses" in loan agreements

and efforts to recover a defaulted loan are restricted to that installments that is currently due, or past due. In the absence of a default provision, agencies cannot enforce full settlement of the loan until all installment payments have come due. Therefore, in the case of loans that span a period of years, the Government is faced with a choice of repeated legal actions to recover installments as they come due or waiting, perhaps years, until all installments are due and taking a single legal action.

Loan agreements frequently do not specify that interest and penalties will be charged on delinquencies. Further, in some guaranteed and insured loan programs, such as the Department of Education's National Direct Student Loan Program, lenders are not required to include standard terms and conditions in loan applications and agreements, thereby weakening the Government's ability to pursue and ultimately collect from the debtor.

Lack of procedures to share
information on credit worthiness

No mechanism exists for sharing information on the credit worthiness of Government debtors. In the private sector, credit bureaus are essential in screening applicants prior to extending credit and in managing outstanding debt. However, there is no mechanism or procedure for sharing credit information on Government debtors among the Federal agencies, among various programs within the same Federal agency, or with the private sector.

Neither the amount of Government credit nor the debtor's payment record with the Government is available. As a result, when a loan application is being reviewed for credit worthiness, agencies

are generally unaware whether the applicant owes other Federal debts, is current in his repayment, or is delinquent or in default to the same or other agencies. The agencies, in effect, must rely upon the honesty of the debtor.

In our recent review of HUD Title I Home Improvement Program, we found that an individual recently obtained seven HUD loans during an eight month period and defaulted on all seven loans. The Debt Collection Project found another individual who had outstanding loans from two different programs in the Department of Agriculture, a Small Business Administration program and an Army Corps of Engineers program, and was in default on all four loans.

Inadequate management of collateral

Certain programs require loans to be secured by collateral to afford some assurance of repayment and greater protection to the Government. Some examples are the HUD Title I housing program, SBA's business loan program, VA's housing program and the Farmer's Home Loan program.

Although our work has been limited in this area, in recent reviews of SBA's business loan program and HUD's Title I Program, we found that:

- Control of collateral was inadequate with the existence, condition, and value often unknown.
- Liquidation practices needed improvement.
- Foreclosure was not used enough as a collection tool.

PROJECTED BUDGETARY SAVINGS
FOR FISCAL 1983

For fiscal 1983, the Administration estimated that \$1.35 billion of debts--accounts and loans receivable--that are now delinquent will be recovered through aggressive administrative actions by the Federal agencies. The \$1.35 billion represents a reduction in outlays which has been distributed to agency accounts. Each agency has been given a collection target for fiscal 1983 and any failure to meet these targets will result in a reduction of the amount of funds an agency has available to spend. At the present time, OMB is developing a system to monitor agencies efforts in meeting these targets.

Another \$1 billion in estimated savings is anticipated in fiscal 1983 budget but has not been distributed to agency accounts. OMB projects that these additional savings could be achieved primarily through enactment of the pending comprehensive debt collection legislation and through intensified Justice litigation efforts.

The Administration also estimates that an additional \$1.66 billion in delinquent taxes will be recovered in fiscal 1983 through an increase in tax collection staff--about 3,000 additional personnel will be allocated to this function--and the development of an automated system for use in IRS's regional offices.

The debt owed the Government has been growing, but we believe these collection estimates are achievable if the Federal Government commits itself to this effort and if the comprehensive debt

collection legislation is enacted. The fact that the Administration has shown its interest by devoting resources to this area and emphasizing debt collection is a good indicator.

This concludes my statement. We will be happy to respond to any questions you or other members of the committee may have.