

BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

9362

The Government Can Collect Many Delinquent Debts By Keeping Federal Tax Refunds As Offsets

Over \$400 million in non-tax receivables was written off by the Government in fiscal 1978, and that amount is increasing. A considerable portion of those non-tax accounts could be collected by reducing future income tax refunds due the debtors. Such an offset procedure would be resorted to only after traditional collection efforts have failed.

IRS' present collection system could be adapted to match refunds with delinquent debts so that the debtor's refund would be retained to cover the debt. This report demonstrates the feasibility of this process and examines the reservations expressed by IRS regarding GAO's proposal.



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To the President of the Senate and the
Speaker of the House of Representatives *CWD 10/10/87*

This report proposes that the Government collect certain delinquent debts by keeping Federal tax refunds as offsets. Currently, over \$400 million in receivables is written off each year because the cost of collection by conventional methods is expected to exceed the amount recovered. However, many of the debts on which collection currently is being terminated could be collected by reducing future Federal tax refunds to the debtor by the amount of the debt.

We made this review because of extensive congressional interest in improving the Government's debt collection procedures.

We are sending copies of this report to the Director, Office of Management and Budget; the Secretary of the Treasury; and the Commissioner of Internal Revenue.

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Comptroller General
of the United States



COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

THE GOVERNMENT CAN
COLLECT MANY DELINQUENT
DEBTS BY KEEPING FEDERAL
TAX REFUNDS AS OFFSETS

D I G E S T

Individuals and businesses owe the Government about \$80 billion and that amount keeps growing. Even though many Government agencies are involved in collecting these receivables, over \$400 million is written off annually because collection is not considered feasible.

The receivables are considered uncollectible because the cost of collection by conventional methods is expected to exceed the amount recovered. However, many of the debts on which collection currently is being terminated could be collected economically by reducing future Federal tax refunds by the amount of the taxpayer's debt.

This method would not replace normal agency debt collection procedures but would be used only as a last resort after the existing debt collection process has proved unsuccessful.

MANY RECEIVABLES ARE PRESENTLY UNCOLLECTIBLE

The allowance for uncollectible receivables as reported by Government organizations to the Treasury as of September 30, 1977, was about \$3 billion. During fiscal 1978, the Government discontinued collection action on over \$400 million in debts to nine agencies. Several other agencies also discontinued collection action on large amounts due the Government. The amounts written off will increase because agencies are accumulating large balances of accounts and loans receivable as a result of overpayments and loan defaults.

Many claims currently being written off are not large enough to warrant recovery through legal action. The fact that collection action

is discontinued does not necessarily mean that the claim is uncollectible. Rather, it means the responsible agency has determined that the current cost of collection will exceed the amount which probably would be collected.

FEASIBILITY OF COLLECTION BY OFFSET

③ Collection of many of the receivables currently written off by the Government as uncollectible could be accomplished by transferring the uncollectible receivable balances to IRS for matching against subsequent tax refunds. In cases where an individual or firm owes the Government money, the applicable tax refund would be reduced by this amount.

To evaluate the feasibility of this offset method, GAO provided data to IRS on 613 outstanding Government receivables valued at \$431,309. IRS determined that \$153,583, or 36 percent, could conceivably have been collected by reducing tax refunds paid in the following 2 years. Additional amounts could have been recovered in succeeding years.

Of the \$153,583 which conceivably could have been collected, \$98,932 was from joint returns. GAO recognizes that IRS can offset individual debts against joint returns only to the extent that the debtor has an interest in the refund. However, in most cases, the debtor will have a substantial interest in the joint refund. (See p. 13).

ALLOWABILITY OF COLLECTION BY OFFSET

④ The Federal Government's right to collect delinquent debts by offsetting against amounts due the debtors is strongly supported by statutes and court decisions. This method would not result in the illegal disclosure of any individual tax return information. (See p. 3).

RECOMMENDATIONS TO THE COMMISSIONER OF INTERNAL REVENUE

The Commissioner of Internal Revenue should implement, on a test basis, procedures which:

--Provide for agencies to refer delinquent receivables to IRS after the agencies have exhausted all collection efforts open to them. These referral procedures, which would include a minimum dollar criteria, could be developed through an interagency task force.

--Screen Federal income tax refunds against these delinquent debts and withhold all or the available part of any refunds due to satisfy the delinquent debts.

Before beginning the test, the Commissioner should advise the Congress of the agency's goals, timeframes for achieving them, methodology, and approach.

★ RECOMMENDATION TO THE CONGRESS

The Congress should provide any funding that may be necessary for IRS to obtain the staffing necessary to accomplish the additional workload imposed by testing and adopting our recommended collection method.

AGENCY COMMENTS AND OUR EVALUATION

The Commissioner of Internal Revenue stated that IRS had reservations about the desirability and practicability of this program when balanced against the value of concentrating IRS resources and expertise on administration of the tax laws. (See p. 18). IRS also felt it could encounter problems in obtaining congressional funding for this program.

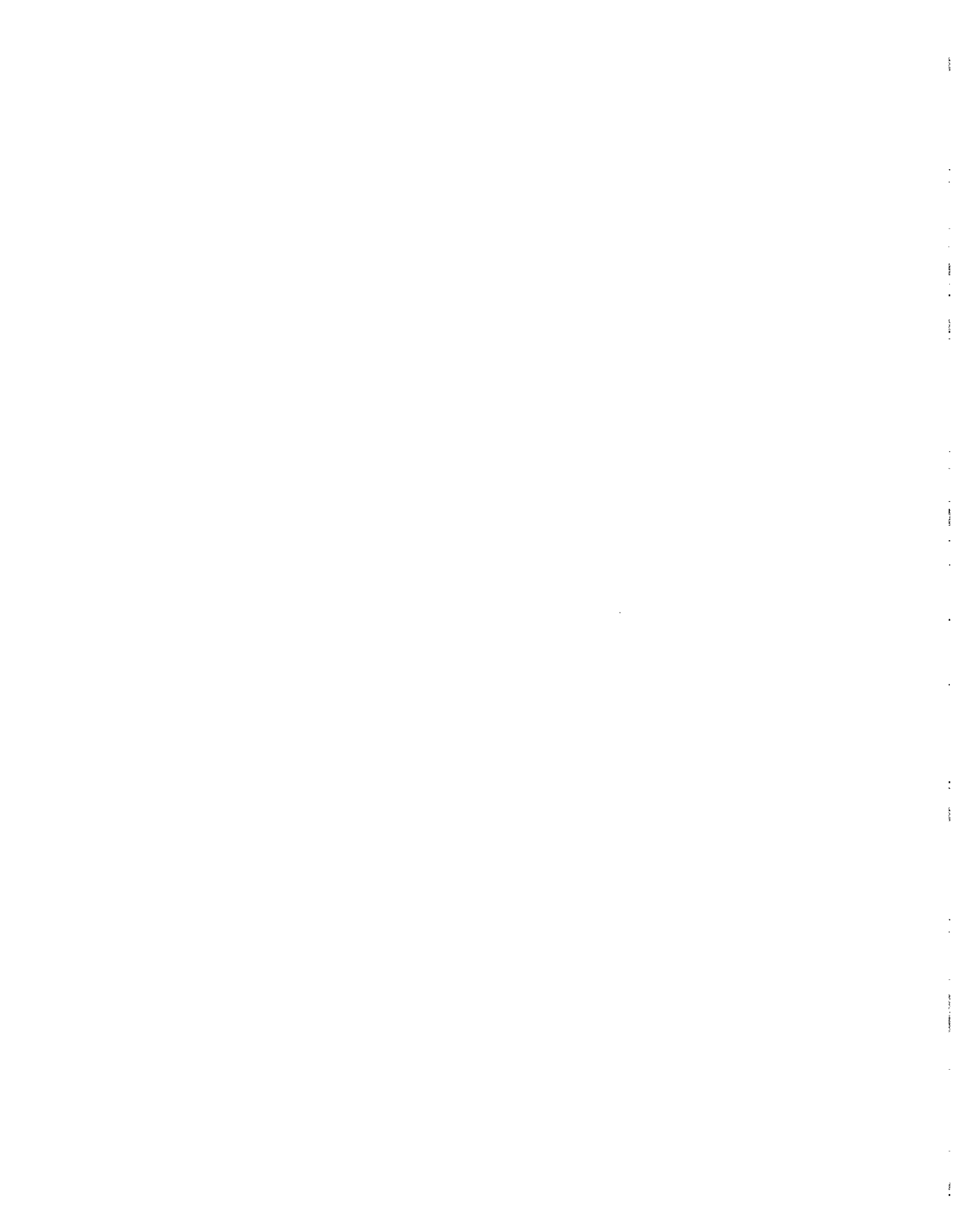
GAO recognizes that sound tax administration is essential to the mission of IRS and that acquiring additional workload while maintaining the present staffing levels could impair tax administration. However, on the basis of GAO's review, the additional personnel necessary to collect by offset would be justified by the substantial amounts that could be collected under this program. (See p. 11).

GAO recognizes that delays can be encountered in obtaining funding for testing and instituting this program and that diversion of resources to this area would temporarily decrease the resources available to administer tax laws. However, these resource limitations should not preclude a test of this program. The test would determine, before undertaking a full-scale program, the extent to which problems exist in this collection method and how they should be overcome.

C o n t e n t s

	<u>Page</u>
DIGEST	i
CHAPTER	
1 INTRODUCTION	1
Many Government receivables not economically collectible using present methods	1
Legality of offset	3
Importance of debt collection efforts	5
Scope of review	5
2 MILLIONS COULD BE COLLECTED BY OFFSETTING DEBTS AGAINST TAX REFUNDS	6
How collection by offset could work	6
Is collection by offset feasible?	8
Why the need for offset will continue	10
3 CONCLUSIONS, RECOMMENDATIONS, AND AGENCY COMMENTS	11
Recommendations to the Commissioner of Internal Revenue	11
Recommendation to the Congress	12
Agency comments and our evaluation	12
APPENDIX	
I Letter dated December 28, 1978, from the Commissioner of Internal Revenue	18
<u>ABBREVIATIONS</u>	
GAO	General Accounting Office
IRS	Internal Revenue Service

ABC 00004



CHAPTER 1

INTRODUCTION

Under current collection practices, Government agencies write off as uncollectible many non-tax receivables which are not in dispute but which are expected to cost more to collect than the amount recovered. That fact was discovered during a previous review ^{1/} and we sought in this review to determine if the Government could economically collect these receivables by withholding the amount due the Government from any future Federal income tax refund due these debtors.

MANY GOVERNMENT RECEIVABLES NOT ECONOMICALLY COLLECTIBLE USING PRESENT METHODS

The value of Government receivables that were written off has increased rapidly in recent years and exceeded \$400 million in fiscal 1978. At September 30, 1977, the accounts and loans receivable as reported by departments and agencies to the Department of the Treasury was about \$118 billion. Excluding foreign debt, the amount was about \$80 billion. The reported allowance for uncollectible accounts was about \$3 billion.

The number and dollar value of uncollectible small claims is expected to increase in the future, as illustrated by the following examples:

--In the fiscal year ended September 30, 1976, the Veterans Administration wrote off about \$66 million as uncollectible. The amount written off increased to about \$85 million in fiscal 1977 and to about \$93 million in fiscal 1978. These uncollectible receivables resulted primarily from overpayments to veterans under educational assistance programs. The average overpayment written off was less than \$500. In addition to the amounts already collected or written off, educational assistance overpayments remaining uncollected as of September 30, 1978, amounted to about \$400 million.

^{1/}"The Government Needs To Do A Better Job of Collecting Amounts Owed by the Public," FGMSD-78-61, Oct. 20, 1978.

--In the year ended September 30, 1977, uncollected overpayments by the Bureau of Retirement and Survivors Insurance, Social Security Administration, increased from \$85 million to \$101 million. Bureau of Disability Insurance reports showed that overpayments increased from \$74 million to \$105 million during the same period.

--In addition to the amounts that have been written off, other Government agencies have accumulated increased amounts of uncollected accounts and loans receivable. For example, the Office of Education has guaranteed over four million student loans amounting to \$4.5 billion through September 1976. The number of these loans held in a defaulted status by the Office of Education has been increasing. From January 1968 to September 1976, about 280,000 defaulted loans accumulated; 76,456 of them in fiscal 1976. Another 147,000 defaulted loans were expected in fiscal 1977. (CD-77-1, Aug. 11, 1977). Loans receivable for this program increased from \$280 million in June 1975 to \$589 million in September 1977.

Government agencies are responsible for collecting all claims of the United States arising from their activities. Criteria and guidance for attempting collection are contained in the Federal Claims Collection Standards issued jointly by the Attorney General and the Comptroller General. Under these Standards, claims which cannot be collected in full may be suspended, compromised, or determined to be administratively uncollectible. Administratively uncollectible claims are either terminated or, if potential for enforced collection exists, referred to us or the Department of Justice. (Some agencies refer these claims directly to Justice while others refer them to us and we may subsequently refer them to Justice.)

Pursuant to the Joint Standards, to refer a claim to the Department of Justice, the amount of the claim generally should be at least \$600. Also, the claim must be accompanied by reasonably current credit data indicating that enforced collection from the debtor can reasonably be expected. Many receivables may therefore be written off because (1) they are less than \$600, (2) available credit data indicates that enforced collection would not be productive, or (3) the Government is unable to obtain current credit data.

Using the above criteria in fiscal 1978, the following Government activities wrote off over \$400 million as uncollectible.

<u>Agency</u>	<u>Amount written off as uncollectible</u>
	(000 omitted)
Small Business Administration	\$152,544
Department of Commerce: Economic Development Administration	10,692
Department of Agriculture: Farmers Home Administration	29,142
Food Stamp Program	1,085
Commodity Credit Corporation	9,523
Department of Housing and Urban Development: Federal Housing Authority	11,088
Interstate Commerce Commission	12,763
Veterans Administration	93,161
Department of Health, Education, and Welfare: Social Security Administration	<u>108,026</u>
Total	<u>\$428,024</u>

Substantial amounts also were written off by several other agencies. Overall statistics on the number and average dollar value of claims written off by the Government were not available. Although most of the amounts written off were the result of Government loan programs and the loan amount usually exceeded \$600, many of the claims written off were not large enough to warrant recovery through litigation.

LEGALITY OF OFFSET

The Government's right to recover delinquent amounts due by offsetting against amounts due the debtor is established in Federal statutes and regulations. 5 U.S.C. 5514 requires agencies to collect overpayments of pay or allowances by offset against future amounts due persons for pay or compensation from the Federal Government. The Joint

Standards promulgated by the Attorney General and the Comptroller General require offset to the extent feasible. 4 C.F.R. 102.3 states that:

"Collection by offset will be undertaken administratively on claims which are liquidated or certain in amount in every instance in which this is feasible. * * * Appropriate use should be made of the cooperative efforts of other agencies in effecting collection by offset * * * and all agencies are enjoined to cooperate in this endeavor."

In enforcing any of these provisions, however, the debtor's rights of due process must be protected.

The Government's right to offset receivables against payables has been tested in the courts. The courts have found that as long as the debtor's due process rights are protected, offset is a proper way to recover a debt owed the Government. Due process requirements are met if the agency referring the receivable for offset

- establishes the validity of the debt,
- notifies the debtor that the receivable is being collected by offset, and
- makes every reasonable effort to give the debtor an opportunity for either a pre- or post-offset hearing.

Although the courts have generally favored offset to collect delinquent receivables due the Government, reducing Federal income tax refunds due debtors is rarely used.

The Internal Revenue Service (IRS) has also recognized the legality of offsetting Government claims against identifiable refunds. Discussions with IRS officials indicate that, notwithstanding the agency's criticism of tax refund offset, IRS has been willing in the past to collect for other agencies by reducing tax refunds when the debtor has a tax refund request pending at the time offset is requested. However, IRS will not offset tax refunds that become due subsequent to the initial request. IRS will also offset individual tax debts against joint refunds to the extent the debtor has an interest (i.e., was responsible for the tax overpayment) in the refund.

IMPORTANCE OF DEBT COLLECTION EFFORTS

The importance of timely and effective billing and collection procedures is recognized by the highest levels of Government. On November 14, 1977, the President announced that his reorganization staff, in conjunction with the Treasury Department, was beginning a comprehensive review of cash management policies, practices, and organization throughout the Federal Government. Among other tasks, the study has paid special attention to how effectively the Government collects money and provides incentives to Federal managers to be more aware of the cash management implications of their decisions.

We have recently performed two reviews of the need to improve the policies and procedures used to establish, control, account for, and collect accounts receivable. Our report on one review (FGMSD-78-61, Oct. 20, 1978) emphasized the need for increased management emphasis on debt collection. In another report, we recommended that agencies increase the productivity of debt collection operations by adopting certain commercial collection practices. (FGMSD-78-59, Feb. 23, 1979)

SCOPE OF REVIEW

Our review was limited to evaluating the feasibility of collecting accounts receivable by reducing future tax refunds. In making this evaluation, we considered past studies performed by IRS. We also obtained the views of IRS on the feasibility of collecting delinquent debts by reducing tax refunds.

We provided IRS with a list of accounts receivable that we determined were economically uncollectible under the present system. This list was limited to those accounts written off during a 1-month period and on which both we and the responsible agency had completed the prescribed conventional collection action. IRS headquarters in Washington, D. C., then determined the extent to which the amounts could have been collected if tax refunds were reduced within 2 years after the accounts were written off.

CHAPTER 2

MILLIONS COULD BE COLLECTED BY

OFFSETTING DEBTS AGAINST TAX REFUNDS

One way of collecting many debts currently written off as uncollectible is to reduce future taxpayer refunds by the amount the taxpayer currently owes the Government. Under the current collection system, many undisputed accounts due the Government are written off as uncollectible because collection is not economically feasible. However, our review of uncollectible claims of several agencies indicated that about 30 percent of those receivables could be collected economically by offset against Federal income tax refunds in the next 2 years.

HOW COLLECTION BY OFFSET COULD WORK

The proposed method of collecting amounts due the Government by reducing future refunds due the taxpayer would work in conjunction with the present collection system. Agencies would retain primary responsibility for collecting any debts due the Government resulting from their operations. They would continue to refer certain claims for legal action. (See p. 2). Once the agencies have determined that further collection action, including legal action, would be unproductive, they would refer the debts to IRS.

Collection of amounts due the Government by reducing pending or future tax refunds would work as follows:

1. The agency would, as now required, pursue collection to the extent such efforts are economically feasible. This collection effort would include documenting the steps taken to notify the debtor and maintaining up-to-date records on debt repayments.
2. After the agency makes every reasonable effort to comply with the due process requirement and exhausts all collection procedures under the present system, the receivables are written off the agency books. This system would not change.
3. However, unlike the present system, collection efforts would not be discontinued when the account is determined to be uncollectible by conventional methods. Instead, the account would be transferred to IRS, and the agency where the receivable was established would not be involved again unless the debtor made a payment to the agency or the

agency collected by offset after collection action was initially terminated. In either case, it would be necessary to advise IRS of the collection.

4. Any further collection effort would be accomplished by IRS and no collection action would be taken until the debtor was due a tax refund. Instead of using its full collection powers as it does to collect tax debts, IRS would place pertinent information about the debt on the taxpayer master file.
5. The taxpayer master file, which identifies the taxpayer by social security number is already screened before any tax refund checks are prepared. The IRS would continue to screen all requests for refunds against its master file as it now does to collect money due to IRS. However, IRS now would determine if an outstanding amount was due the Government for non-tax debts at the time the request for refund was screened against the master file.
6. The refund would then be reduced by the amount of the debt up to the full refund amount and the debtor taxpayer would be informed of the action taken. In those instances where an individual incurred the debt but filed a joint return, IRS would decide how much to offset against the refund based on the extent that the debtor was responsible for the tax overpayment. Spouses filing a joint return have separate interests in any refund due. The refund is apportioned to a spouse to the extent that he or she contributed to the overpaid tax. Only the portion of the refund which belongs to the debtor would be retained by the Government. This method of determining ownership of refunds is currently used by IRS.
7. IRS would not attempt to collect debts that are less than an established minimum amount and would not retain debtor information indefinitely. After the system design work is completed, a cost study should be made to determine the minimum dollar criteria that should be used in referring claims to IRS. Also, after the system has been implemented for a number of years, criteria would be developed for eliminating items from the master records.

Although this method of collection would use existing IRS equipment and money collected would be deposited in the Treasury as general receipts, certain details would have to be worked out. A procedure would be needed to transfer to IRS

those accounts written off by each agency. Developing this procedure would include identifying the specific information required by IRS, such as name, social security number, amount due, and how the debt was incurred. In addition, a mechanism would have to be established to provide the data to IRS in computer compatible format. Also, controls assuring that IRS is notified of any debts paid to the agency after referral must be established. An interagency task force could develop all these procedures.

IS COLLECTION BY OFFSET FEASIBLE?

No Federal statute prohibits offset of a tax refund against a non-tax debt. Therefore, the Government may collect amounts due by reducing Federal income tax refunds.

To help evaluate the feasibility of this method of collection, we requested assistance from IRS which determined the offset potential of 613 accounts that were owed to the Government. These receivables totaled \$431,309, and both we and the responsible agencies had completed all prescribed collection actions. The fact that a claim was written off does not mean that the debt was uncollectible, but rather that we and the responsible agency either

- were not able to locate the debtor,
- were not able to collect any substantial portion of the debt, or
- expected the cost of collection would exceed the amount recovered.

In any event, since some of the uncollectible debts were not large enough to warrant recovery through litigation and legal action was not considered feasible on others, the Government could not economically enforce collection under the existing procedures.

Of the \$431,309 in uncollectible accounts, IRS data indicated that \$153,583, or 36 percent, could conceivably have been collected by reducing tax refunds which were paid for tax years 1974 and 1975. The amount that conceivably could have been collected is shown in the tables on the following page.

Returns with Refunds

<u>Amount of liability</u>	<u>1974</u>		<u>1975</u>	
	<u>Number</u>	<u>Amount</u>	<u>Number</u>	<u>Amount</u>
\$1-\$249	52	\$ 8,647	14	\$ 1,572
\$250-499	159	40,487	90	11,024
\$500-999	92	28,524	69	14,843
\$1000-1499	35	13,348	32	13,846
Over \$1499	<u>33</u>	<u>10,218</u>	<u>29</u>	<u>11,074</u>
Total	<u>371</u>	<u>\$101,224</u>	<u>234</u>	<u>\$52,359</u>

A further analysis of the data provided by IRS showed that a high percentage of the small debts could have been collected by offset. This is illustrated by the following schedule.

<u>Amount of liability</u>	<u>Claims written off</u>		<u>Claims collectible by offset in 2 years</u>	
	<u>Number</u>	<u>Amount</u>	<u>Amount</u>	<u>Percent</u>
\$1-249	84	\$ 16,433	\$ 10,219	61
\$250-499	249	88,104	51,511	58
\$500-999	165	114,234	43,367	38
\$1000-1499	53	66,279	27,194	41
Over \$1499	<u>62</u>	<u>146,259</u>	<u>21,292</u>	15
Total	<u>613</u>	<u>\$431,309</u>	<u>\$153,583</u>	36

Although we believe this test demonstrates the feasibility of offsetting non-tax debts against tax refunds and indicates that over 30 percent of the debts included in the test could potentially have been offset, we recognize that the percentage of debts collected when the proposed offset system is implemented may be somewhat different. These variances in collection rates could be caused by two situations.

Of the \$153,583 which conceivably could have been collected, \$98,932 was from joint returns. We recognize the individual debts can only be offset against joint return

refunds when the debtor has an interest in the refund; that is, the debtor contributed to the tax overpayment. However, in the majority of cases, the debtor will have a substantial interest in the tax refund.

This test was limited to a 2-year period. It is logical to assume that additional amounts could be recovered in succeeding years. However, at some point, it would no longer be feasible to retain debts on the IRS system for further collection effort. That cutoff point would have to be determined after the system is in operation.

WHY THE NEED FOR OFFSET WILL CONTINUE

In a recently published report, we recommended improved debt collection practices and procedures and emphasized the need for agencies with primary responsibility for debt collection to increase the management emphasis placed on this area. 1/ In another related review, we evaluated adopting certain commercial practices to increase the productivity of debt collection operations. 2/

One of the most significant problems in collecting receivables is a shortage of trained staff to handle the collection workload. Another is that the population of this country is mobile and locating debtors has become more difficult. In addition, some U.S. attorneys are reluctant to take collection action against recipients of overpayments, so they give these cases a low priority. Among the reasons cited for the low priority were (1) the relatively small amount of Federal money lost in individual cases, (2) an inadequate number of personnel to develop documentation, and (3) too few U.S. attorneys to handle the cases. Also, Justice believes that the court systems are already overburdened, and other ways are needed to deal with small cases.

1/"The Government Needs To Do A Better Job of Collecting Amounts Owed By The Public," FGMSD-78-61, Oct. 20, 1978.

2/"The Government Can Be More Productive In Collecting Its Debts By Following Commercial Practices," FGMSD-78-59, Feb. 23, 1979.

CHAPTER 3

CONCLUSIONS, RECOMMENDATIONS, AND AGENCY COMMENTS

The Government can reduce its losses from bad debts by establishing a program to collect delinquent debts by reducing tax refunds. Our tests showed that many debtors who refuse to pay amounts due the Government receive a Government tax refund. Because collection by reducing tax refunds is economically feasible, this collection method should be used as a final administrative attempt to recover amounts due the Government from those who have successfully evaded agency collection efforts.

We recognize that certain complications may arise in obtaining the funding necessary to adopt this collection method and that diversion of resources to the collection of non-tax amounts due decreases the resources available to administer the tax laws. Therefore, we are recommending implementation of this system on a test basis. This manner of implementation will enable IRS to find out the extent to which there are problems and how they should be overcome before undertaking a full-scale program.

RECOMMENDATIONS TO THE COMMISSIONER OF INTERNAL REVENUE

We recommend that the Commissioner of Internal Revenue implement, on a test basis to evaluate their cost effectiveness, procedures which:

- Provide for agencies to refer delinquent receivables to IRS after the agencies have exhausted all collection procedures open to them. These referral procedures, which would include a minimum dollar criterion, could be developed by an interagency task force.
- Screen Federal income tax refunds against these delinquent debts and withhold all or the available part of any refunds due to satisfy the delinquent debts.

Before beginning the test, the Commissioner of Internal Revenue should advise the Congress, of the agency's goals, time frames for achieving them, methodology, and approach.

To keep the Congress fully informed of the status of this test effort and of the resources used on this project, the goals, time frames, methodology, and approach should be closely coordinated with the appropriate committees. To get the test started as soon as possible, it should probably be

restricted to a single agency. This agency would refer its uncollectible accounts to IRS for actual collection in accordance with the procedure described in chapter 2. IRS would post these non-tax debts to the master file and then screen this file before tax refund requests are processed. When an amount is due the Government for non-tax debts at the time a refund is due the taxpayer, the refund would be reduced by the amount of the debt up to the full refund amount. The taxpayer would be informed of the action taken.

After a reasonable period, such as 2 years, the results of this offset test would be evaluated. At that time, the extent of any problems with this system would be identified and any necessary changes to the system would be made before expanding the program to all agencies.

RECOMMENDATION TO THE CONGRESS

The Congress should provide any funding that may be necessary for IRS to obtain the staffing necessary to accomplish the additional workload imposed by testing and adopting our recommended collection method.

AGENCY COMMENTS AND OUR EVALUATION

The Commissioner of Internal Revenue, in a December 28, 1978, letter, stated that IRS did not find that the results of our review supported the desirability and practicability of this proposed offset program when balanced against the value of concentrating IRS resources and expertise on the administration of tax laws. IRS raised the following objections to collection by this means.

Debtors can adjust withholding

The proposed system would not work if debtors adjusted their withholding to avoid collection of non-tax debts. IRS believes that the perceived benefits from this type of proposal would be short-lived because the taxpayers can reduce or eliminate overwithholding or cause underwithholding and thus eliminate the availability of refunds to be offset.

We agree that the extent to which debtors will adjust their withholding cannot be predicted. However, at the present time, about 80 percent of those who file tax returns receive refunds and in fiscal 1977 about 67.9 million individuals received \$36.5 billion in tax refunds.

Although many taxpayers can take action to reduce withholding by filing an Employee's Withholding Allowance Certificate they must certify under penalty of perjury

that they do not owe Federal income taxes for last year and that they do not anticipate incurring a tax liability for the current year. This limitation on adjustment of withholding should deter underwithholding. Therefore, we do not believe that a substantial number of debtors would take action to reduce or eliminate overwithholding.

Availability of joint refunds

Returns of those individuals who file jointly with persons who are not liable for the debt may be unavailable for offset. IRS stated that data was not available to show the extent to which debtors would have an interest in joint refunds. Also, IRS stated that it did not know the cost of developing an administrative system that would allow the agency to determine, on a massive scale, the amount of interest a debtor had in refunds from joint returns.

Although our analysis of the data provided by IRS was based on the assumption that all refunds on joint returns would be available for offset, we recognize that these refunds would be available for offset only to the extent that the debtor was responsible for the tax overpayment. In a majority of cases, however, we believe the debtor would be the person responsible for a substantial part of the tax overpayment. This opinion is based on a review of 1976 Department of Labor statistics. Most debtors are male, and the statistics show that for married families, 82 percent of the males and 45 percent of the females are in the workforce.

As IRS stated, the cost of developing an administrative system to determine the interest of debtors in joint refunds is unknown. However, since we are recommending that this proposal be implemented first on a test basis, such data should be available after the test.

Correct social security numbers are needed

Refunds are not available for offset if the social security number of the debtor is unavailable or incorrect because taxpayers cannot be matched with their refunds without it. IRS stated that the availability and accuracy of social security numbers for the debtors is essential.

We agree that claims should not be referred to IRS when the debtor's social security number is not known. However, as collection of outstanding receivables has become more sophisticated, greater use is made of social security numbers, and on current cases, it is unusual for the debtor's correct social security number to be unknown.

Past studies were inconclusive

IRS stated that previous indepth feasibility tests on the use of offset conducted by IRS for the Departments of Agriculture and Justice were inconclusive and did not, in the opinion of IRS, justify the use of offset.

We agree with IRS that the previous tests were inconclusive. The test conducted for the Department of Agriculture was designed to determine the feasibility of placing primary responsibility for collecting and enforcing repayment of overissued food stamps on IRS. The proposed legislation, which initiated this test, would have provided machinery for annual recoupment of the value of food stamps when the recipient's taxable income exceeded specified limits. The collection actions presumably would have included seizure of property and court actions to enforce liability. The ability of IRS to collect overpayments in the manner we are proposing was not evaluated during the Agriculture study.

The study exploring the feasibility of IRS using individual income tax refunds to offset Justice Department judgment debts was a more valid test of offset potential. Tax records for the Southern New York and Eastern Michigan regions for 1968 through 1971 were compared to the inventory of Justice Department judgment debts on hand in December 1969. Based on the study criteria, returns of individuals who subsequently filed joint returns were not considered susceptible to offset. Secondly, the offset rate against large debts was much lower than against small debts since individual refunds during the test period averaged about \$250 per year.

This study showed that, in the two regions reviewed, the offset potential varied considerably and was significantly greater for relatively small judgment debts. Only 2.6 percent of the aggregate dollar value could have potentially been collected in the region having judgment debts averaging \$6,700 each. In the other region, where debts averaged \$1,800, 27 percent of the aggregate dollar value of the judgment debts could conceivably have been collected in the 4-year period. This study also showed that collection of all or part of about 60 percent of the judgments under \$500 was possible in both regions using only individual returns.

Revision of computer programs

IRS stated that the impact of modifying the computer programs to implement this proposal would be major because

of a severe shortage of resources. Also, the tax administration was considered to be of higher priority than the non-tax debt collection operation.

Under the proposed system, non-tax debts would be posted to the taxpayer master file in the same manner as tax debts. The IRS already posts tax debts to the taxpayer master file, and this file is screened before any tax refund check is processed. Some revisions would have to be made to the computer programs that screen refund requests; but these revisions would be relatively minor and should not present any serious computer processing problems.

Although we did not evaluate the availability of IRS resources to revise computer programs, we believe a change of this nature should be given a high priority. Responsible IRS personnel estimated that this computer program change would require about one-half of a staff-year. The potential collections received by implementing this proposal on a test basis would, in our opinion, justify this expenditure of resources.

Privacy Act limitations

Information on the amount of refund to which an individual is entitled is confidential under the Internal Revenue Code and the Privacy Act of 1974. Thus, IRS could not disclose the amount of, or existence of, overassessments for the purpose of offset. Our proposal that IRS furnish statistical information on collections only to the responsible agencies has not received congressional consideration.

However, we have no reason to believe that the Congress would be opposed to IRS providing that information to the responsible agencies. The use of the proposed collection system would not be precluded by restrictions on disclosure of the amount of money collected from specific taxpayers, and IRS would be able to disclose statistical information on the degree of success of the collection program without violating disclosure laws.

An individual would not be restricted, under the proposed system, from disclosing that a debt had been collected by IRS. If an individual applied for additional benefits from the same agency that referred his or her uncollectible debt to IRS, the agency would collect by offset when feasible. The individual would be responsible for providing proof to the agency of the amount collected by IRS.

Impairment of tax administration

IRS believes that taxpayer relations would be damaged if the "policing of debtors" were widely publicized. This use of IRS records for satisfying debts due other agencies could have an adverse impact on the tax administration system. Also, IRS questioned the possible inequity of shifting the costs of a legal defense to those who question the debt's validity or amount.

IRS also commented that relying upon additional funding from the Congress to implement the proposed system presented unacceptable administrative risks. This reservation was based on previous IRS experience in obtaining congressional funding for computer system initiatives.

We recognize that acquiring additional workload while maintaining the present staff could impair tax administration, but we believe that by increasing personnel to perform this new function, current work would not be greatly affected.

We have recognized that delays may be encountered in obtaining the funding necessary to implement this proposed collection method. However implementing this system on a test basis will reduce the administrative risks taken by IRS.

In addition, we are not suggesting that offset be used as a replacement for normal agency debt collection procedures, but rather that offset be used as a final administrative attempt to recover monies due the Government from debtors who have successfully evaded agency collection efforts. Agencies would still pursue debtors and consider litigation to collect delinquent receivables, but agencies would refer delinquent receivables to IRS after administrative collection attempts were exhausted and if the cost of litigation would exceed the amount of the debt. Therefore, the number of taxpayers involved in offset action would be small in relation to the total number of taxpayers since the offset procedure would be used only if all other collection efforts fail.

A widespread public outcry against using IRS as the Government's debt collector should not be heard if offset is used under the constraints discussed. Instead, quite the opposite reaction would likely occur if this collection procedure were publicized. The majority of honest citizens who pay their debts to the Government would be gratified to see the Government taking action to recover delinquent debts.

Also, any debts of questionable validity or amount would not be referred to IRS. Instead, the agency having

cognizance over the receivables would be responsible for referring only well-defined debts to IRS for offset.

We believe collection by offset is warranted by equity concerns. It is patently unfair to the honest citizen who pays his debts to the Government to allow other debts to go uncollected. This inequity is especially acute when the individual owing the debt has the ability to pay but does not, and the validity or amount of the debt is not in dispute.

After considering the reservations expressed by IRS, we still believe the Government should collect debts by reducing future tax refunds. Thus, we believe our recommendations should be implemented.

COMMISSIONER OF INTERNAL REVENUE

Washington, DC 20224

DEC 28 1978

Mr. Allen R. Voss
Director, General Government Division
General Accounting Office
Washington, DC 20548

Dear Mr. Voss:

We believe the best interests of sound tax administration conflict with the recommendation, in your draft report entitled "Delinquent Non-Tax Amounts Due Should Be Collected By Reducing Federal Tax Refunds to Debtors", that the Service establish a computer system attempting to deduct from tax refunds the debts which other federal agencies find uncollectible by "conventional" methods. We find the evidence in your draft report insufficient to establish the desirability and practicability of this program, when balanced against the value of concentrating our resources and expertise on the administration of the tax laws.

We believe that your finding that about 36 percent of \$431,000 in 613 uncollectible accounts ". . . could conceivably have been collected by reducing tax refunds . . ." does not support our embarking on an attempt to deal with what appears to be a \$3 billion inventory of uncollectible non-tax accounts increasing \$200 million annually, the number and average dollar value of which are unknown. Our reservations about the justification for your recommendation are:

1. The system you propose would not work if debtors adjusted their withholding to avoid collection of their non-tax obligations. You ". . . are unable to predict the extent to which people will adjust their withholding." We know that withholding is an underpinning of our tax administration system, that our problems of collecting tax where there is substantial underwithholding would be significant and that your proposal would offer a tempting incentive to cause underwithholding. We are not prepared to run the risks to which a massive non-tax debt collection program would expose the withholding system.

Mr. Allen R. Voss

2. Your test found that \$98,932 of the \$153,583 which "conceivably" could have been collected was from joint returns. A premise of your recommendation is that ". . . in most cases, GAO assumes that the debtor will have a substantial interest in the joint refund." We do not know the basis for your assumption. Notwithstanding our ruling position, neither do we know the cost or feasibility of developing an administrative system to determine on a massive scale the interest of debtors in refunds from joint returns.
3. You recognize that the system depends on referring claims where the debtors' social security number is known, but we do not know the basis for your conclusion that this information is "usually" known by the responsible agency, to what extent the information is accurate, or the costs which would be involved in perfecting inaccurate data.
4. Previous tests of this type of proposal going back to 1968 data are inconclusive. As you point out, only 2.6 percent of the judgment debts potentially could have been collected in one region and 27 percent in another over a hypothetical four year period, assuming debtors did not adjust their withholding to avoid collection. It does appear that collecting judgments under \$500 would be more likely than collecting larger judgments.
5. You assume that computer program revisions to implement the program would be ". . . relatively minor and should not present any serious computer processing problems." We believe the impact would be major in terms of our severe shortage of Data Services resources. Moreover, we would rank the needs of our scarce Data Services resources for tax administration purposes higher in priority than their use in a non-tax debt collection operation.

Mr. Allen R. Voss

6. Congressional policy in protecting the privacy of tax data limiting the data's use to tax administration purposes except as specifically provided has produced legislation with narrowly drawn allowances for use of tax information to collect non-tax debts. These special provisions permit disclosure of a taxpayer's address for collection of a debt under the Federal Claims Collection Act of 1966 and for collection of student loans. Your suggestion for avoiding our concerns about protecting the confidentiality of return information under the law by your proposal for our furnishing only statistical information on collections to responsible agencies has not received Congressional consideration.
7. Our concerns that using the Service to collect what would essentially be small non-tax debts could impair our primary mission are unrelieved by your recommendation that we acquire more personnel to perform this new task and your conclusion that the public reaction would be gratification at the equity of collecting these bills through the tax administration system. The equity of setting off tax refunds against debts not large enough to warrant the Federal Government's costs of recovery through legal action must be balanced against the possible inequity of shifting the costs of a legal defense to those who question the debts' validity or amount. Moreover, your study indicates that 61 percent of debts below \$250, but only 15 percent of the debts over \$1,499 might have been collected by offset. Yet the debts in your study below \$250 represented only 3.8 percent ($\frac{\$16,433}{\$431,309}$) of the total dollar value of claims in your sample, while claims over \$1,499 represented 33.9 percent ($\frac{\$146,259}{\$431,309}$) of the uncollectible accounts which you studied.

Mr. Allen R. Voss

Your suggestion that we establish procedures to implement the program, while coupled with your recommendation that the Congress provide funding, does seem to us to present unacceptable administrative risks. You reason: "No federal statute prohibits offset of a tax refund against a non-tax debt. Therefore, the Government may collect amounts due by reducing Federal income tax refunds." However, our experience in obtaining Congressional funding for computer system initiatives leads us to be opposed to implementing a massive, doubtful and unproven non-tax program as the Federal Government's bill collector of last resort. Moreover, if the policy objective is to offset uncollectible debts to the Government against payments to those debtors by the Government, then perhaps a more comprehensive survey of Government payments to its debtors (including those delinquent in their tax obligations) should be made rather than focusing only on refunds payable by the tax administration system.

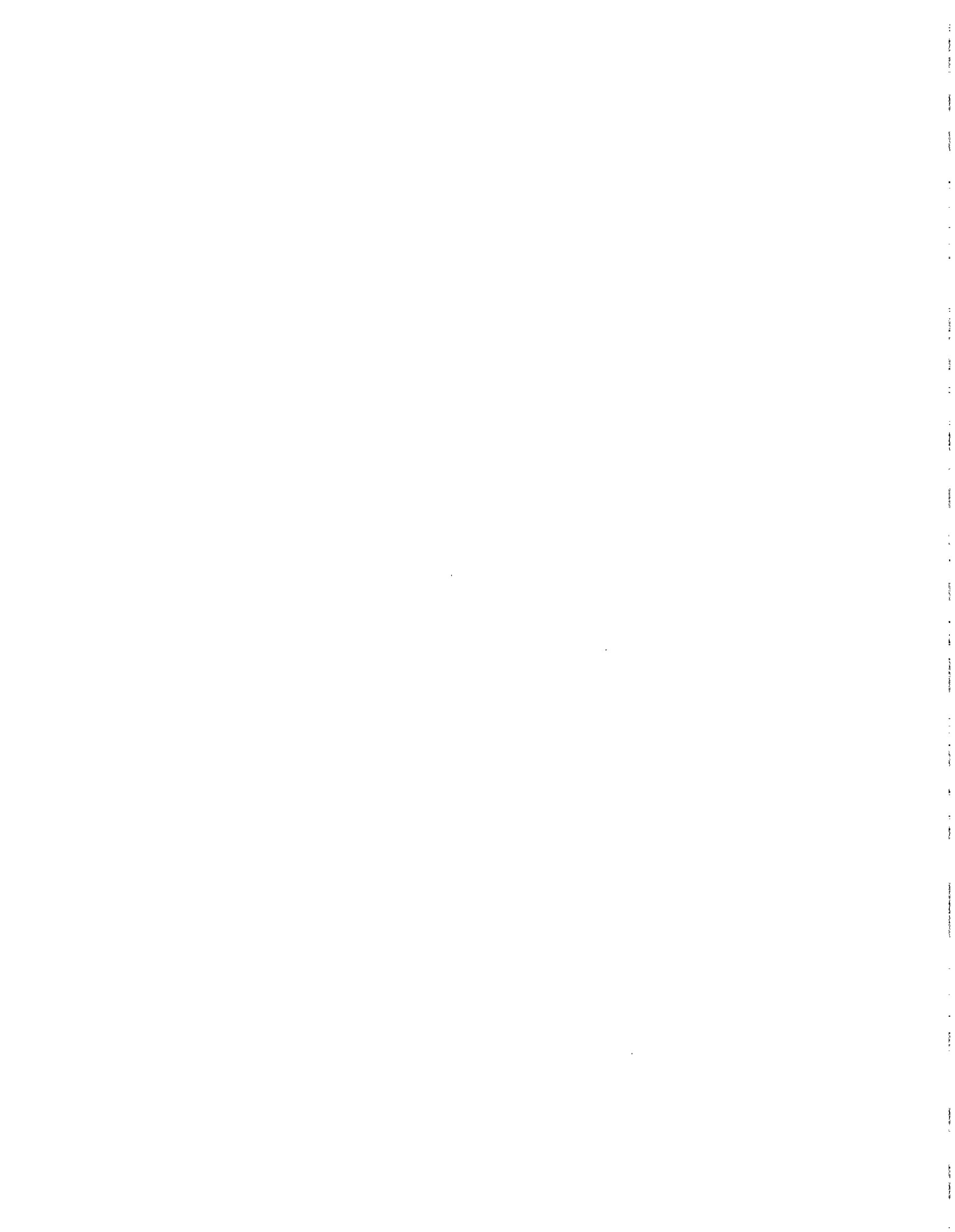
We appreciate this opportunity to comment on your draft report.

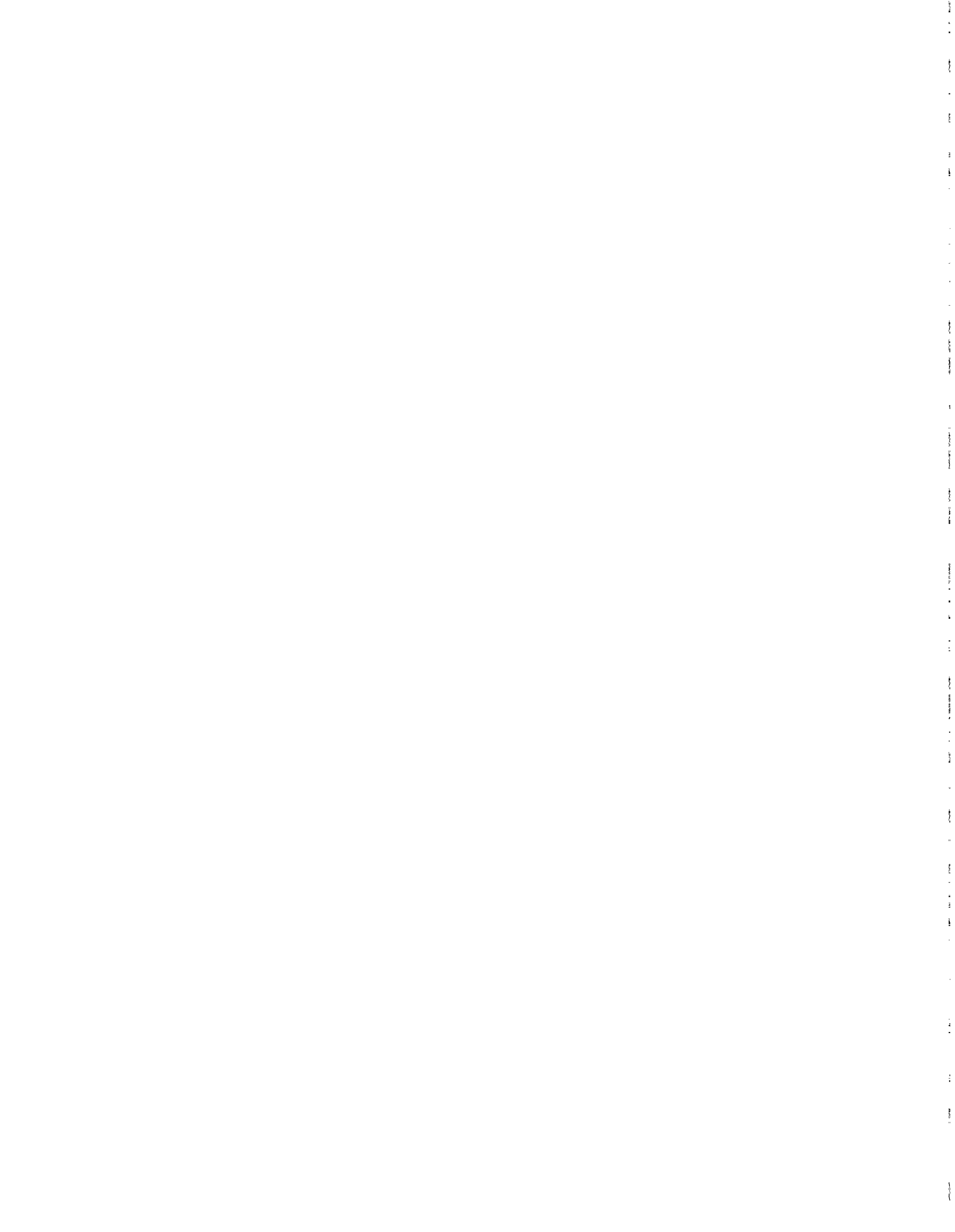
Sincerely,

A handwritten signature in cursive script, appearing to read "James K. ...". The signature is written in black ink and is positioned below the word "Sincerely,".

(90117)







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