STATEMENT OF COMMISSIONER KENNETH R. PAPAJ
U.S. DEPARTMENT OF THE TREASURY
FINANCIAL MANAGEMENT SERVICE
BEFORE THE UNITED STATES SENATE
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

Tuesday, March 20, 2007
Washington, DC

Chairman Levin, Ranking Member Coleman, and Subcommittee members, thank you for inviting me here to testify today. I'd also like to take this opportunity to thank the members of this subcommittee for your ongoing support of the Financial Management Service's (FMS) and the Internal Revenue Service's (IRS) efforts to improve and strengthen the Federal Payment Levy Program and for your continued interest in ensuring that federal contractors meet their tax obligations. I am pleased to report that as a result of your vigilance and initiative our combined efforts are paying off.

Levy Collections Continue to Increase

Collections of delinquent taxes through the Federal Payment Levy Program have increased dramatically over the last several years. As this first chart illustrates, the total amount of levy collections has more than tripled, from $89.3 million in fiscal year 2003 to $303.3 million in fiscal year 2006. There has been continued growth in collections from every type of payment that is part of the levy program – vendor, federal salary, federal retirement, social security benefit, and non-Treasury disbursed vendor payments. With regard to levy collections from federal contractors, as chart 2 illustrates, collections increased from $7.0 million in fiscal year 2003 to $59.6 million in fiscal year 2006 (chart 2). These increases are due to significant improvements in the program, some of which I will discuss today. More importantly, through future initiatives, and by working closely with the IRS and other agencies, we fully anticipate increases in levy collections to continue. In fact, FMS is on track in fiscal year 2007 to exceed last year's record tax levy collections.

The Number of Tax Debts Referred to FMS has Increased

One major contributing factor to the increase in levy collections is the increase in the number of tax debts that IRS has made part of the levy program. As of December 31, 2006, FMS' system showed more than $111.9 billion in delinquent taxes that were eligible for matching against federal payments (chart 3). This represents an increase of $53.1 billion in tax debt since the end of 2003. Of this amount, IRS has activated $55.1 billion or 49% for collection by levy. Debts that have been activated for collection are those for which IRS has completed the notice and review process which is legally required prior to levy. We continue to work closely with the IRS to have them activate more tax debts for levy because as the collection trends indicate, levy collections increase as more debts are activated for collection.

In an attempt to increase the number of debts activated for collection by levy, the Administration has proposed a legislative change that would permit IRS to conduct post-levy due process under certain circumstances. We believe this change could significantly increase collections particularly with regard to payments to federal contractors. In the meantime, however, through the hard work of the Federal Contractor Tax Compliance Task Force, systems have been put in place to identify federal contractors who owe taxes which enables the IRS to accelerate the collection due process in those cases.

More Payments are Being Levied

Another significant factor contributing to increased levy collections has been an increase in the types of payments that are being matched and levied against delinquent tax debts under the Federal Payment Levy Program. The first major expansion of the program took place in January, 2002 with the addition of social security benefit payments. In December 2002 we began adding payments made to Department of Defense contractors and by April 2005 all of the multiple Department of Defense vendor pay systems were incorporated into the program. In February, 2003, salary payments issued by the United States Postal Service were added and beginning in April 2004, Department of Defense salary payments were made available for levy. I am pleased to report that FMS is now in the process of adding the vendor payments of the U.S. Army Corps of Engineers and the U.S. Postal Service to the levy program, both of which are planned for implementation this June. Test matches show potential collections of $106.4 million from Corps of Engineers contractors and $164.5 million from Postal Service contractors.

Additionally, FMS has been working to ensure that our various systems for making payments to vendors, Type A, Automated Clearing House-Corporate Trade Exchange (ACH-CTX) and Fedwire, are included in the levy program.

Type A payments are typically made by agencies that do not have the payment volume to support sending large-scale bulk payment files. ACH-CTX payments are for multiple payments to the same payee or one payment with multiple invoices which allow transmitting complete remittance information with the payment. The Fedwire payment system is used for low-volume, high dollar transactions that are deposited into recipients' bank accounts on the same business day.

We began levying some Type A Payments in January 2006 and full implementation was completed in June 2006. I am pleased to report that ACH-CTX and Fedwire payments are on schedule for full implementation into the levy program by the end of December 2007.

We have also been working hard with federal agencies to ensure that the payments that are part of the Federal Payment Levy Program have complete information that is necessary for the levy to take place. All agencies for which we disburse are now 100% compliant with the requirement to complete the name field on payments files and most agencies are 95% to 100% compliant with the requirement to include a taxpayer identification number (TIN). We continue to work closely with those few agencies that have not yet reached a satisfactory TIN compliance rate.

One of the concerns of this Subcommittee has been the use of purchase cards by agencies to pay vendors who owe taxes. FMS, along with the General Services Administration (GSA) and the IRS, is in the process of implementing a task force recommendation that will prevent contractors who owe delinquent debt from being paid for contracts through the use of the purchase card. This will be accomplished by identifying and flagging in the Central Contractor Registration system those contractors that have debts and paying them using payment methods that are subject to levy. We anticipate that FMS' programming to implement this recommendation will be completed in the next month. Draft changes to the Federal Acquisition Regulations (FAR) have been completed and are under review by the FAR Council. Once the changes to the FAR are finalized, use of the flag by contracting officers will begin

Reciprocal Agreements With States

Another initiative which has been of interest to this subcommittee is our efforts to enter into reciprocal agreements with states. These agreements will allow for the administrative offset of federal payments to collect debts owed to states and the corresponding offset of state payments to collect debts owed to federal agencies. An interim rule governing this program was published on January 11th 2007 and a pilot program is scheduled to begin with the three states that expressed interest in participating - Maryland and New Jersey in the Spring, followed by Kentucky later this year. We are already seeing results as the state of New Jersey has informed us that it has collected about $6.4 million in business tax debts over the last three months as a result of sending notices about the initiation of this administrative offset program. If these pilots prove successful and cost beneficial, FMS will renew its efforts to bring additional states into this program.

Levy of CMS Payments

With regard to Medicare payments issued by the Department of Health and Human Services' Center for Medicare and Medicaid Services (CMS), as GAO acknowledged both when they first began to examine the Federal Payment Levy Program and again in their most recent analysis, due to CMS' decentralized payment process there are significant operational complexities associated with adding these payments to the Federal Payment Levy Program. Additional complexities arise because of the role CMS' fiscal intermediaries play in the payment process. However, as CMS moves to consolidating its processes it is now feasible to address the issue of levying CMS payments.

Working under the direction of the Federal Contractor Tax Compliance Task Force, a subgroup consisting of FMS, IRS, and CMS has been formed to determine how best to deal with Medicare providers who are delinquent on their tax obligations. I join my colleagues from IRS and CMS in supporting the work of the task force to examine various options to ensure that payments to Medicare providers are levied in the most efficient and effective manner. Some options that should be evaluated are improving the paper levy process already in place between IRS and CMS; establishing a matching program between CMS' fiscal intermediaries and either IRS or FMS to facilitate levies through the fiscal intermediaries; and having FMS disburse Medicare payments on behalf of CMS so that levies can be conducted using the existing Federal Payment Levy Program. Each of these options presents logistical, operational and technical issues that must be worked out. Once the task force has completed its analysis it will issue a report by the end of the year setting forth the various options and making recommendations for levying payments to Medicare providers who fail to satisfy their tax obligations. FMS is fully committed to working, through the task force, toward this important goal.

While it is our view that we do not currently have the legal authority to offset Medicare payments to collect nontax debt (including delinquent child support obligations), concurrent with examining solutions to the operational complexities associated with levying Medicare payments, we would also examine offset options, in consultation with the Department of Health and Human Services.

Mr. Chairman, once again, I appreciate the invitation to discuss the role FMS has played and will continue to play in improving the Federal Payment Levy Program and in helping to close the tax gap. FMS is very proud of its accomplishments in debt collection which, in fiscal year 2006 resulted in record collections of over $3.3 billion and since inception of the program has yielded collections of more than $29.5 billion in delinquent tax and nontax debt owed to federal agencies and states that otherwise would not have been collected.

This concludes my remarks and I would be happy to answer any questions.

Chart 1

Tax Levy Collections

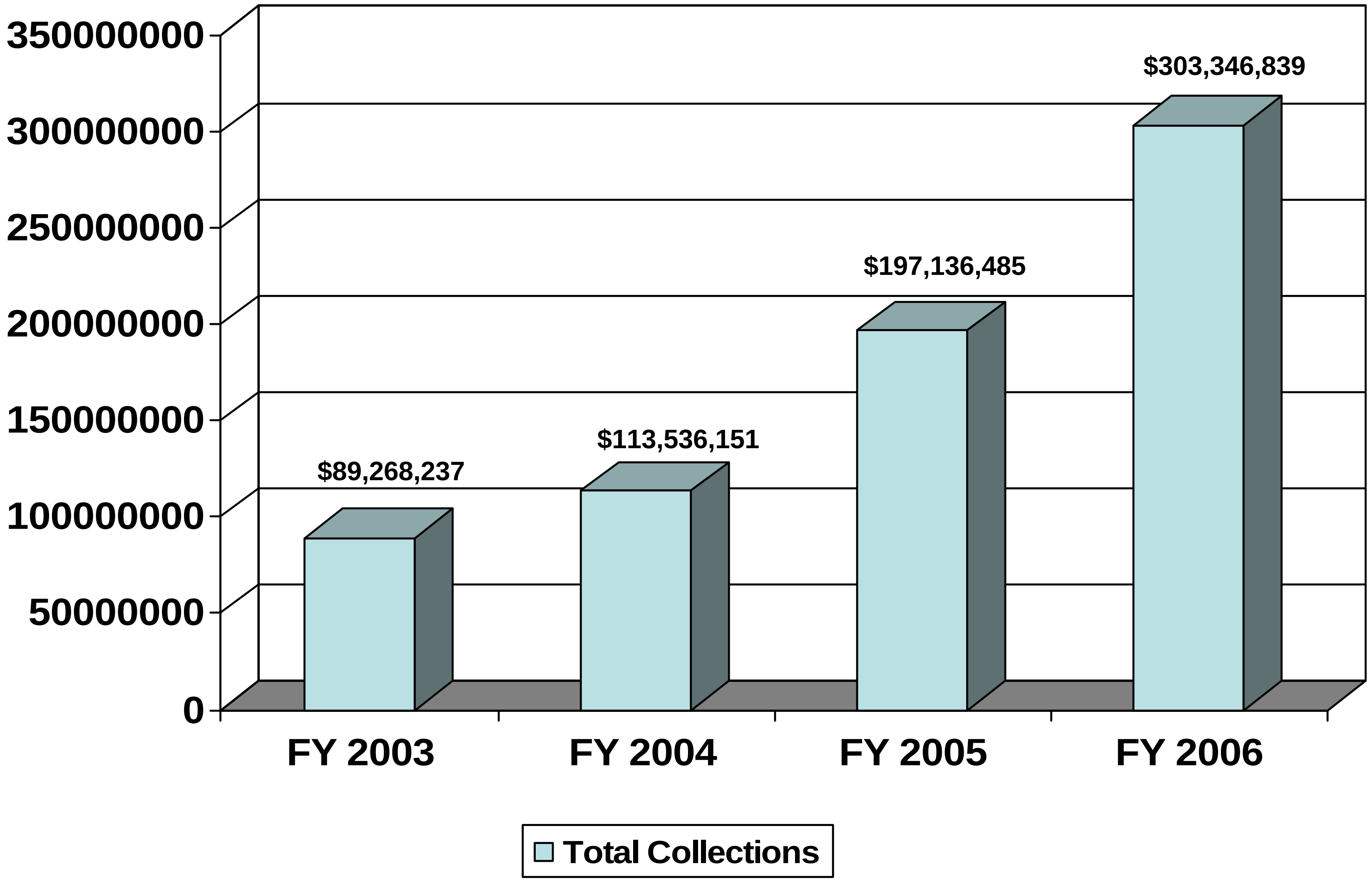
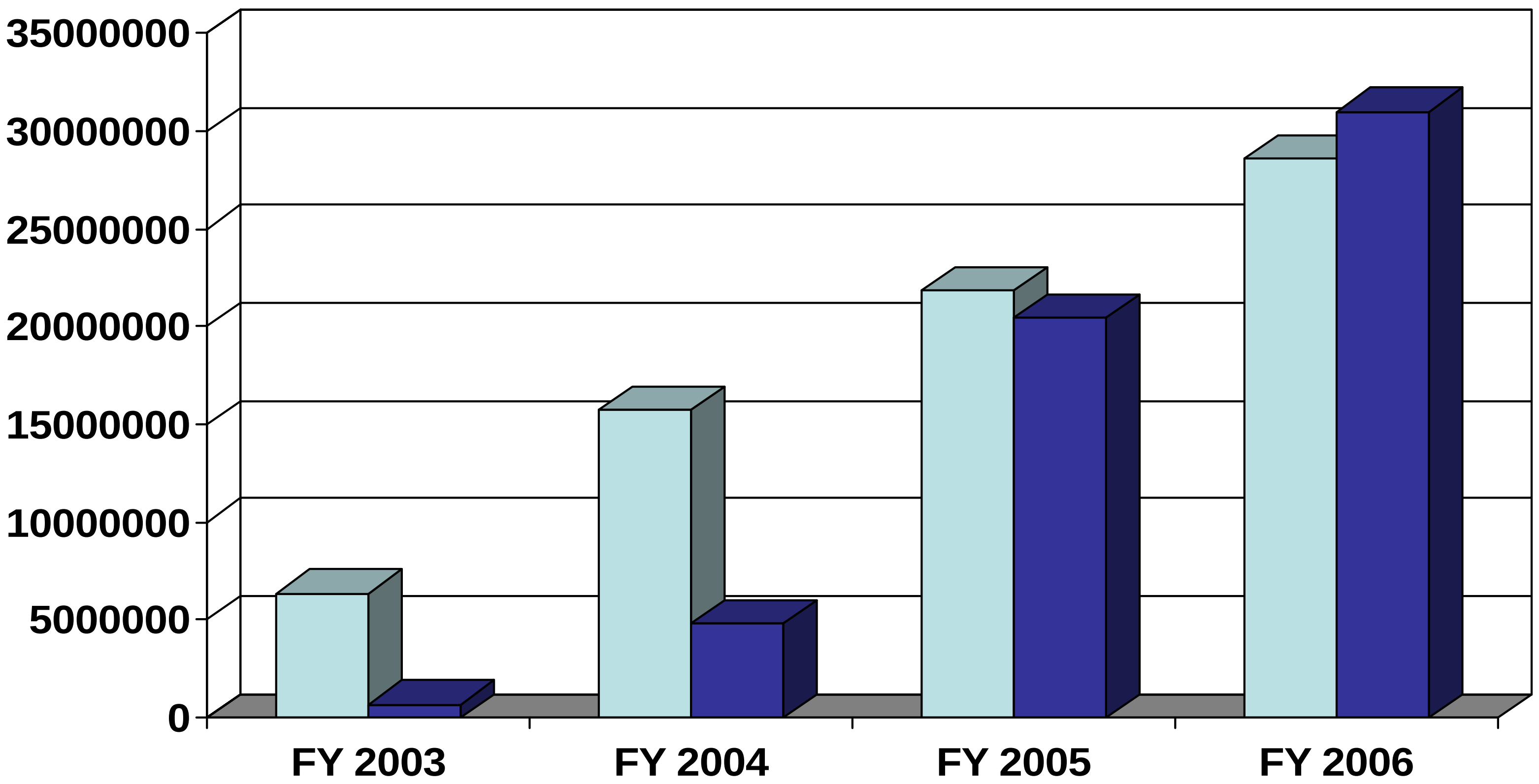


Chart 2

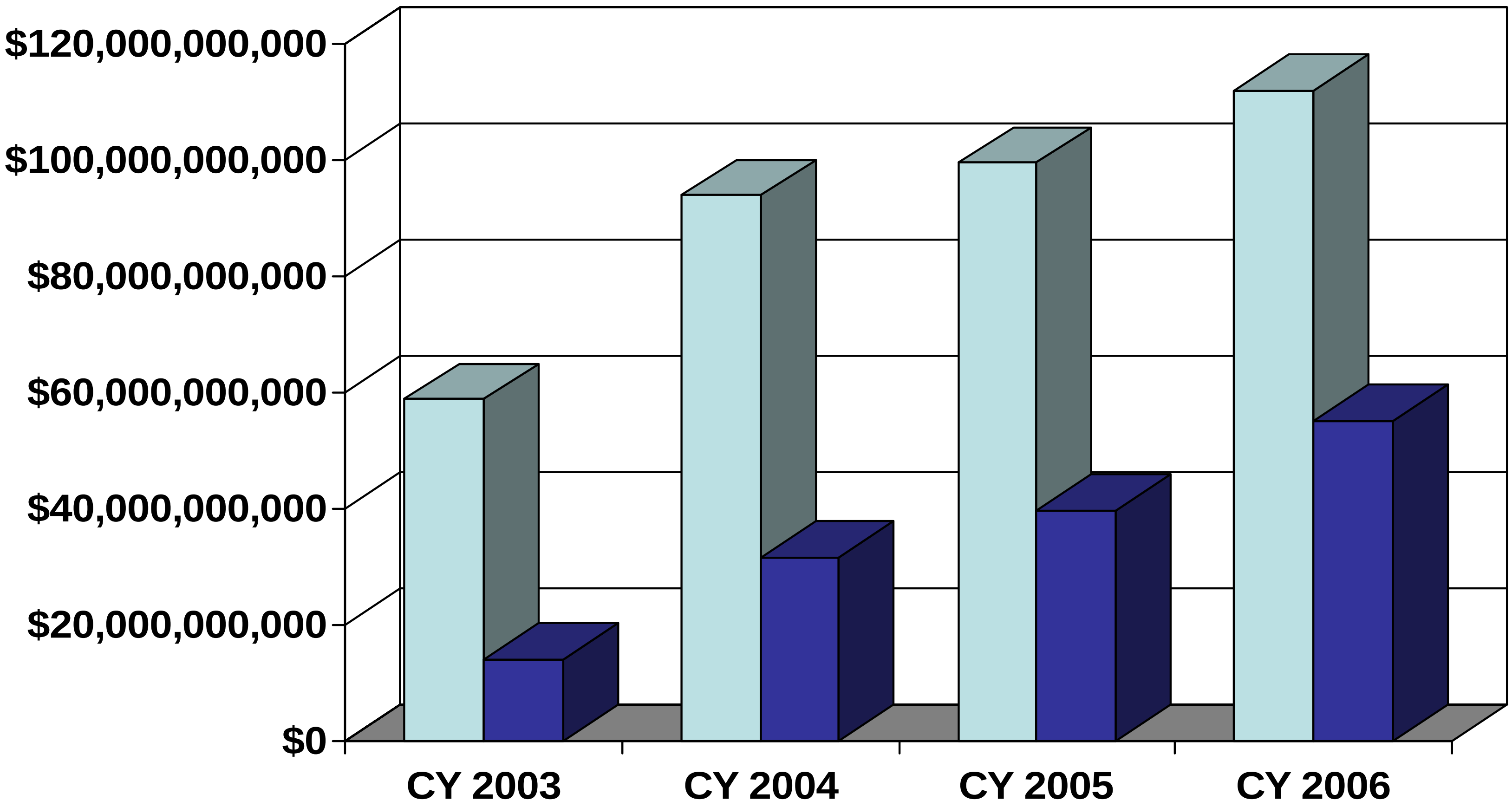
Vendor/DoD Vendor Collections



	FY 2003	FY 2004	FY 2005	FY 2006
Vendor	$6,356,137	$15,709,086	$21,858,013	$28,591,679
DoD Vendor	$686,888	$4,774,361	$20,424,920	$31,018,485
Total Vendor	$7,043,025	$20,483,447	$42,282,933	$59,610,164

Chart 3

Tax Levy Debts



	CY 2003	CY 2004	CY 2005	CY 2006
Debts Eligible for Matching	$58,713,323,574	$93,909,200,632	$99,471,193,903	$111,891,914,135
Debtors Activated for Levy	$14,060,648,969	$31,537,277,515	$39,661,414,415	$55,114,007,727
Percentage Activated	24%	33%	40%	49%