

HJR

41

# SENATE COMMITTEE REPORT

DATE: 4/9/08

FURTHER:

DATE TURNED  
IN TO OFFICE: \_\_\_\_\_

State Affairs Committee considered CS FOR HOUSE JOINT RESOLUTION NO. 41(RLS)

HJR 41 REPEAL OF SEC. 511 OF P.L. 109-222

Urging the United States Congress to repeal sec. 511 of P.L. 109-222 (Tax Increase Prevention and Reconciliation Act of 2005).

and recommends:

- be replaced with  SCS or  CS \_\_\_\_\_ ( )
- adopt previous  SCS or  CS \_\_\_\_\_ ( )
- attached amendment(s)
- adopt \_\_\_\_\_ Letter of Intent
- further referral to \_\_\_\_\_ Committee

**SENATE BILL:**  
 Same Title  
 New Title

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**HOUSE BILL:**  
 Same Title  
 Technical Title Change  
 New Title w/ SCR # \_\_\_\_\_

**NEW FISCAL NOTE(S):**

Department	Date	Fiscal	Indet.	Zero	FN#

**PREVIOUS FISCAL NOTE(S):**

Department	Date	Fiscal	Indet.	Zero	FN#
Admin	4/8/08			✓	

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	PRINTED LAST NAME	DO PASS	DO NOT PASS	NO REC	AMEND
	Bundo			✓	
	Green	✓			
	French	X			
	French			✓	
CHAIR:	Melburn	✓			

*Member*

*Standing Committees:*  
Judiciary  
State Affairs

*House Special Committee:*  
Ways & Means

*Finance Subcommittees:*  
Administration  
Courts

# Alaska State Legislature

## House of Representatives



**Representative Max F. Gruenberg, Jr.**  
**House District 20**

Anchorage (Mountain View, Russian Jack, East Anchorage)  
House Minority Assistant Floor Leader

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### **SPONSOR STATEMENT FOR HJR41**

#### **BY: REPRESENTATIVE MAX F. GRUENBERG, JR.**

This resolution urges Congress to repeal sec. 511 of P.L. 109-222, the Tax Increase Prevention and Reconciliation Act of 2005.

This provision was added by a congressional conference committee without benefit of any public hearings in either the House or Senate.

If this provision remains law, starting in 2011 it will require states and local governments that spend more than \$100 million each year on goods and services to withhold three percent of the price of those goods and services and transmit those funds to the IRS to apply to any taxes that may be owed by vendors.

Section 511 was enacted to save approximately \$7 million in federal taxes between 2011 and 2015. However, the effect of that law would increase the burden and costs to state and local governments by making them uncompensated and involuntary federal tax collectors, because no federal funding is provided.

Government officials have stated that this provision will be extremely difficult and expensive to implement, requiring major programming changes to their financial and accounting systems and the hiring of additional staff. The state's accounting system is 23 years old, and the state has had difficulty avoiding mandatory backup withholding, which would be costly and time-consuming. This provision would make mandatory withholding even more difficult to avoid.

Local businesses would be discouraged from bidding on state and local governmental contracts, because of the three percent withholding. This would dampen competitive bidding and probably raise prices to the state and local government.

# FISCAL NOTE

**STATE OF ALASKA**  
**2008 LEGISLATIVE SESSION**

Fiscal Note Number: 1  
 Bill Version: HJR 41  
 ( ) Publish Date: 4/8/2008

Identifier (file name): \_\_\_\_\_ Dept. Affected: ADM  
 Title Urging the United States Congress to repeal sec. 511 of P.L. 109 RDU \_\_\_\_\_  
 Sponsor House Rules Component \_\_\_\_\_  
 Requester \_\_\_\_\_ Component Number \_\_\_\_\_

**Expenditures/Revenues** (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

	Appropriation Required	Information						
		FY 2009	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
<b>OPERATING EXPENDITURES</b>								
Personal Services								
Travel								
Contractual								
Supplies								
Equipment								
Land & Structures								
Grants & Claims								
Miscellaneous								
<b>TOTAL OPERATING</b>		<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

<b>CAPITAL EXPENDITURES</b>								
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<b>CHANGE IN REVENUES ( )</b>								
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**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts								
1003 GF Match								
1004 GF								
1005 GF/Program Receipts								
1037 GF/Mental Health								
Other Interagency Receipts								
<b>TOTAL</b>		<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

Estimate of any current year (FY2008) cost: 0.0

**POSITIONS**

Full-time								
Part-time								
Temporary								

**ANALYSIS:** (Attach a separate page if necessary)

Prepared by: Rachelle Fenderson, House Rules Committee Aide  
 Division: House Rules Committee  
 Approved by: Representative John Coghill, Chairman  
House Rules Committee

Phone 465-3719  
 Date/Time 4/8/08 4:30 PM  
 Date 4/8/2008

## **Government Alliance to Repeal 3% Withholding**

Section 511 of the Tax Reconciliation Act (PL 109-222) requires that federal, state and local governments withhold 3% on payments made for most goods and services. However, the implementation of the new directive raises several issues for state and local governments.

**Unfunded Mandate:** The provision would impose significant costs which have been determined to exceed the threshold, making the legislation an unfunded mandate.

**Increased Financial and Administrative Commitments:** Implementation of the new provision would impose significant financial and administrative commitments for state and local governments. Many governments do not have systems that can handle a large increase in additional information reporting or that contain modules that can withhold and remit monies for each payment made. Even governments with more robust systems would have to undergo significant changes to their current software, which would entail additional administration and personnel. In most cases, significant modifications and/or new software would be required. Many government payment systems are antiquated. Furthermore, more category codes and greater complexity and processing would be needed to accommodate the exemptions, and in most cases, manual intervention would be necessary, thereby increasing the cost of implementation.

**Additional Staff and Education:** Even if the current systems could be amended or new systems could be purchased, additional staff resources will be necessary to carry out the new requirement. New duties would include reconciliation of withholdings and subsequent payment to the federal government, preparation of tax deposits, monitoring of agency payments, and increased compliance monitoring (i.e., lots of training necessary). Additional FTEs would also be required to track down payment errors, handle bad addresses, monitor changes in the law, and field telephone calls from vendors.

**Increased Recordkeeping:** The provision would require additional recordkeeping to track the required withholdings. Additionally, vendor files would need to be significantly expanded to accommodate all payments.

**Increase in Cost for Goods and Services:** Companies will simply pass the 3% withholding along in increased prices when dealing with governments. In turn, bids to governments will be higher and smaller businesses competing for government business will be at an unfair disadvantage.

**Competitive Disadvantage:** Because only governments and not private sector businesses are required to withhold 3%, governments will be at a significant disadvantage over private sector buyers, as vendors may choose not to contract with governments particularly when selling high-demand or scarce goods.

**Cannot Withhold on Payments Made by Purchase Card:** In order to implement the provision for purchase cards, buy-in from credit card companies would be necessary,

which in turn would raise the per transaction costs for governments. Standard credit card process would need to be significantly amended. Additional fees are anticipated. Furthermore, issues arise as to whether a payment would be exempt if using a purchasing card since in reality the bank is technically making the payment.

**IRS Capacity Questionable:** Additional reporting and withholding issues raise questions about the IRS's capacity to rectify withholding with corporate tax returns. The current lack of enforcement and staffing make it unlikely that a large increase in withholding and reporting could be enforced without a significant increase in resources.

**Mechanisms to Collect Taxes and Punish Bad Actors are Already in Place – The Federal Government is Passing on Collection Responsibility to Lower Levels of Government:** Essentially, state and local governments are being forced to act as tax collectors for the federal government. The provision to withhold 3% on payments is passing on collection duties from the federal government to the state and local levels. The provision is essentially a tax on vendors providing services to governments. Existing tax collection mechanisms have not been adequately enforced.

**The \$6 Billion Estimated Tax Collection is an Acceleration of Receipts – Actual Collection is About \$215 Million Per Year:** The provision is an attempt to increase collection from vendors who are not paying taxes. The \$6 billion estimate in the first year is actually the 3% withheld amount and does not consider reconciliation with corporate tax returns, which is shown in year two and thereafter to generate only \$215 million.

**Bill History/Action for 25th Legislature**

**BILL:** HJR 41

**SHORT TITLE:** REPEAL OF SEC 511 OF P.L. 109-222

**BILL VERSION:**

**CURRENT STATUS:** (H) RLS

**STATUS DATE:** 04.07.08

**SPONSOR(s):** RULES

**HEARING:** (H) RLS Apr 08 4:00 PM CAPITOL 120 Moved CSHJR 41(RLS) Out of Committee

**TITLE:** Urging the United States Congress to repeal sec. 511 of P.L. 109-222 (Tax Increase Prevention and Reconciliation Act of 2005).

Bill Number:

Jm-Date	Jm-Page	Action
04.07.08	2699	(H) READ THE FIRST TIME - REFERRALS
04.07.08	2699	(H) RLS
04.07.08	2699	(H) REFERRED TO RULES

Similar Subject Match or Exact Subject Match

INTERGOVERNMENTAL RELATIONS

MUNICIPALITIES

PUBLIC FINANCE

TAXATION

Bill Number:

[Return to Basis Main Menu \(25th Legislature\)](#)



# STATE OF ALASKA

DEPARTMENT OF ADMINISTRATION

ANNETTE KREITZER, COMMISSIONER

SARAH PALIN, GOVERNOR

P.O. BOX 110200  
JUNEAU, ALASKA 99811-0200

PHONE: (907) 485-2200

FAX: (907) 485-2135

April XX, 2008

The Honorable  
United States Senate  
Washington, DC 20510

Dear Senator XXXX,

As Commissioner of the Department of Administration for the State of Alaska, I am writing to express the State of Alaska's strong support for repealing Section 511 of the Tax Increase Prevention and Reconciliation Act (TIPRA) of 2006, which requires governments to withhold 3% on payments made for most goods and services.

If enacted, Section 511 of TIPRA will impose an enormous burden on state and local governments, most of which do not have the systems or capacity to implement this onerous and costly withholding provision. Additionally, it will place governments at a competitive disadvantage as private sector businesses do not have to comply with this requirement.

As a state finance official, I have grave concerns regarding the impact of this poorly vetted provision on the current accounting and procurement systems in my state. Preliminary research indicates that not only will implementation costs be significant and include both administrative and financial commitments, but also that governments will face an increase in the costs of goods and services as vendors will simply pass along the 3% cost when bidding for government business.

I oppose Sec. 511 as an unfunded mandate and disagree with this new policy of shifting the burden of federal tax collection to state and local governments. I strongly urge you to support repealing this provision.

Sincerely,

Annette Kreitzer

Fact Sheet

## Repeal Three Percent Withholding Tax on County Purchases

**Issue:** Section 511 of the Tax Increase Prevention and Reconciliation Act (P.L. 109-222) requires counties that spend more than \$100 million annually on purchases to withhold and remit to the IRS three percent of most payments for products and services.

**NACo policy:** NACo supports repeal of Section 511 of P.L. 109-222. This is among NACo's key federal legislative priorities for 2007.

**Action needed:** County officials should urge their members of Congress to cosponsor H.R. 1023 (Rep. Kendrick Meek, D-Fla., and Rep. Wally Herger, R-Calif.). This bill would repeal Section 511 of P.L. 109-222.

**Background:** H.R. 4297, the "Tax Increase Prevention and Reconciliation Act of 2006", was signed into law as P.L. 109-222 on May 17, 2006. Section 511 will require many counties beginning in 2011 to withhold federal taxes on nearly every payment for a service or product – from plumbing services to paper clips - with no minimum transaction and regardless of whether the payment is made by check or credit card. The requirement does not apply to the private sector. It is estimated to raise \$6 billion for the federal treasury through a first-year accounting gimmick and slightly more than \$200 million per year thereafter.

According to the Congressional Budget Office, this is an intergovernmental mandate with costs above the threshold of the Unfunded Mandates Reform Act. It will be very expensive for counties to implement and will require programming changes to financial and accounting systems and the hiring of additional staff. It will also likely discourage contractors from bidding on government contracts and increase the costs of procurement. Many of its requirements are unworkable as written and will require the Treasury Department to issue 'administrability rules'. This mandate is particularly egregious because it was inserted into the final version of an omnibus tax bill that had already passed both the House and Senate and was never subject to a formal vote, hearings or consultation with any state and local government officials or their national organizations.

On February 13, 2007, Representatives Kendrick Meek (D-Fla.) and Wally Herger (R-Calif.) introduced H.R.1023 to repeal this unfunded mandate on county government. NACo is asking members of Congress to cosponsor this legislation. It is important to demonstrate broad support for this legislation because it faces an uphill climb due to its \$7 billion price tag.

For further information, contact: Alysoun McLaughlin 202/942-4254 or [amclaughlin@naco.org](mailto:amclaughlin@naco.org).



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*Advocacy: the voice of small business in government*

August 31, 2006

VIA FACSIMILE and EMAIL

The Honorable Larry E. Craig  
United States Senate  
520 Hart Senate Office Building  
Washington, DC 20510

RE: S. 2821 *Withholding Tax Relief Act of 2006*

Dear Senator Craig:

I am writing to express support for your legislation, S. 2821, the *Withholding Tax Relief Act of 2006* (S. 2821). This legislation will repeal section 511 of the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222) (TIPRA). The withholding provision in TIPRA is a broad new requirement mandating that federal, state and local governments withhold 3 percent from payments made for goods and services. Small business groups have expressed a high level of interest in S. 2821 to the Office of Advocacy (Advocacy). Advocacy takes its direction from small business groups which is why we are writing this letter of support.

Congress established Advocacy under Pub. L. 94-305 to represent the views of small businesses before Federal agencies and Congress. Advocacy is an independent office within the U.S. Small Business Administration (SBA), so the views expressed in this letter do not necessarily reflect the views of the SBA or the Administration.

Section 511 of TIPRA presents significant challenges for small entities and state and local governments. American small businesses operate in an environment which challenges them to be competitive and remain profitable. The withholding provision will impede the cash-flow of small entities, presenting another obstacle to their success. Section 511 of TIPRA amounts to a tax penalty on government contractors without a clear path for reimbursement. The amount of the penalty is variable; for instance if a contract generates a small profit or no profit the additional withholding presents serious cash management challenges. Additionally, the

withholding provision inhibits the efficient use of capital because it will limit funds that can be used to reinvest in the business.

In fiscal year 2005, the Federal government spent over \$300 billion purchasing goods and services from businesses. Purchases from small businesses represented almost \$80 billion. Two-thirds of the Federal government procurement falls under the Department of Defense (DOD). The Government Accountability Office (GAO) issued a report entitled "DOD Payments to Small Businesses" (GAO-006-358, May 2006). GAO concluded that disruptions in cash flow caused by contracting with DOD can significantly affect the day-to-day operations of small businesses. Adding a 3 percent tax withholding requirement will only exacerbate the cash flow issues already experienced by small entities seeking to do business with the government.

In addition to the burdens that may be imposed on small businesses by the withholding provision, section 511 of TIPRA may have unintended administrative costs on all levels of government required to collect the tax. The withholding requirement at a minimum will require changes to be made to the accounting methods and software used by governmental jurisdictions. That may be why the Congressional Budget Office described the withholding provision as an unfunded intergovernmental mandate.

Repealing section 511 of TIPRA will help small businesses maintain their ability to provide goods and services to governments at all levels. Thank you for your efforts on behalf of small businesses. Advocacy looks forward to working with you and Congress to repeal this provision.

Sincerely,

/s/ \_\_\_\_\_  
Thomas M. Sullivan  
Chief Counsel for Advocacy

# Government Withholding Relief Coalition

Join the Coalition

Home

## Government Withholding Relief Coalition (GWRC)

The Government Withholding Relief Coalition (GWRC) was formed to repeal a sweeping new requirement mandating that federal, state, and local governments withhold 3 percent from payments for goods and services. This unprecedented withholding mandate will affect all government contracts as well as other payments, such as Medicare and grants, starting in 2011. Section 511 of the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222) enacted this requirement into law.

### Coalition Letters

- [July 17, 2007 - Letter to House Ways and Means Committee](#)
- [March 22, 2007 - Statement for the Record to House Small Business Committee](#)
- [March 12, 2007 - Letter to Senator Craig in support of S. 777](#)
- [March 8, 2007 - Letter to Treasury Department](#)
- [February 15, 2007 - Letter to Rep. Meek and Herger in support of H.R. 1023](#)
- [January 17, 2007 - Letter in opposition to use of 3% withholding as an offset](#)
- [October 16, 2006 - Letter to Representative Herger in support of H.R. 6242](#)
- [July 11, 2006 - Letter to Senator Craig in support of S. 2821](#)

### Department of Treasury Solicitation for Comments on Implementation: Due April 28

- [Treasury's Notice 2008-38](#)

### Resources

- [One-page summary of provision](#)
- [Talking Points](#)
- [Draft Letter to Congress for Businesses to Utilize](#)

### Material

- [June 12, 2007 - Senators Collins and Coleman Letter](#)
- [March 13, 2007 - Dear Colleague letter in support of S. 777 - Senator Craig](#)
- [February 22, 2007 - Dear Colleague letter in support of H.R. 1023 - Rep. Meek and Herger](#)
- [September 19, 2006 - Letter from Senator Craig to Senate colleagues in support of S. 2821](#)
- [August 31, 2006 - Letter to Senator Craig from SBA Office of Advocacy in support of S. 2821](#)
- [May 9, 2006 - CBO Letter with Annual Budgetary Effects](#)

### Bills to Repeal Provision

- [Senate - S. 2894 \(110th Congress\)](#)
- [Senate - S. 777 \(110th Congress\)](#)

- House - H.R. 1023 (110th Congress)
  - Senate - S. 2821 (109th Congress)
  - House - H.R. 6242 (109th Congress)
-



# Municipality of Anchorage

P.O. Box 196650 • Anchorage, Alaska 99519-6650 • Telephone: (907) 343-4431 • Fax: (907) 343-4499 <http://www.muni.org>

Mayor Mark Begich

Office of the Mayor

April 3, 2008

The Honorable Max Gruenberg  
Alaska House of Representatives  
State Capitol, Room 110  
Juneau, AK 99811

Dear Representative Gruenberg:

I write to commend you for your sponsorship of a resolution urging repeal of a federal tax provision in the Tax Increase Prevention and Reconciliation Act of 2005, which is certain to have a detrimental effect on the Municipality of Anchorage and other government entities across our state. I also thank you for bringing this misdirected provision to our attention.

This provision would require cities and other government entities across the nation to withhold a 3 percent payment from nearly all vendors and contractors for federal income tax purposes, if it becomes effective in 2010 as currently intended. As your measure correctly points out, this could cause chaos to Anchorage's finance and computing systems, costing taxpayers thousands of dollars a year.

We support your call for repeal of this provision and again thank you for pursuing this important resolution in the current legislative session.

Sincerely,

Mark Begich  
Mayor

*Community, Security, Prosperity*



## *Issue Brief:* New Government Withholding Provision Could Involve Costs to States

National Association of State Budget Officers

October 3, 2006

444 N. Capitol Street, Suite 642 • Washington, DC 20001 • (202) 624-5382 (phone) • (202) 624-7745 (fax) • [www.nasbo.org](http://www.nasbo.org)



### **BACKGROUND**

On May 17, 2006, the *Tax Increase Prevention and Reconciliation Act of 2005* was signed into law. Major elements of this law include extending the fifteen percent tax rate on capital gains and dividends, and preventing an increase in the number of taxpayers subject to the Alternative Minimum Tax. Another important component of the law that received far less publicity, but could impact state and local governments, requires governments to withhold three percent on certain payments to persons providing property or services. The provision will not go into effect until 2011.

#### **Specifics of Withholding Provision**

The withholding provision extends the act of withholding to new areas. Under the withholding provision, all levels of government are required to withhold three percent on most payments for products and services. According to the summary provided by the Senate Finance Committee, the provision "requires withholding on certain payments to any person providing property or services made by the Government of the United States, every State, every political subdivision thereof, and every instrumentality of the state." Governments would then be required to remit three percent of most payments to the federal government for federal income tax purposes. The withholding provision will go into effect on January 1, 2011.

Prior law states that employers are required to withhold income tax on wages paid to employees, including wages paid to employees of federal, state, and local government. This law has not previously included withholding payments to workers who are not classified as employees, such as independent contractors. Instead, independent contractors and other taxpayers who receive income that is not subject to withholding are required to make estimated tax payments.

There are some exemptions to the withholding provision. First, localities and other political subdivisions of states with less than \$100 million of annual expenditures for goods or services are exempt from the withholding requirement. Second, the provision exempts payments made through a federal, state, or local government public assistance or public welfare program for which eligibility is determined by a needs or income test. Finally, the provision exempts payments of interest, payments for real property, payments to tax-exempt entities or foreign governments, intergovernmental payments, payments based on a classified or confidential contract, and payments made to a government employee not otherwise excludable with respect to their service as an employee.

#### **Reasons for Withholding Provision**

The main stated justification for the withholding provision is to attempt to undermine the misreporting of taxes by certain government vendors not currently subject to withholding. It is one of a series of steps designed to help minimize the tax gap. According to the IRS, in 2001 taxpayers paid \$345 billion less than what they should have paid. This caused the Joint Committee on Taxation (JCT) to produce a report in 2005 entitled *Options to Improve Tax Compliance and Reform Tax Expenditures*. The first recommendation of the report was to impose withholding on certain payments made by government entities. The JCT contended that a lack of a withholding requirement on non-wage payments leads to substantial underpayment of taxes each year. Additionally, the JCT argued that requiring withholding on government entities for non-wage payments would improve taxpayer compliance, promote fairness, and reduce the tax gap. According to government estimates, the withholding provision will raise \$7 billion for the federal government between 2011 and 2015.

#### **ISSUES RAISED REGARDING WITHHOLDING PROVISION**

State and local groups have begun to raise numerous concerns about the withholding provision. The law is vague in many areas, and specific regulations have yet to be established. Further details regarding the implementation of the withholding provision will be determined by the Department of Treasury. Currently, many state and local government associations are monitoring developments regarding the withholding provision. In addition to NASBO, these associations include the National Governors Association (NGA), the National Association of Counties (NACo), the National Association of State Auditors, Comptrollers, and Treasurers (NASACT), the National Conference of State Legislatures (NCSL), the National League of Cities (NLC), the United States Conference of Mayors, the Federation of Tax Administrators (FTA), the National Association of State Retirement Administrators (NASRA), and the Government Finance Officers Association (GFOA). Some of the primary issues that have been raised concern:

- **Unfunded mandate** – As reported by the Congressional Budget Office (CBO), the Joint Committee on Taxation (JCT) has determined that the cost of the withholding provision exceeds the threshold specified in the *Unfunded Mandates Reform Act*.
- **Costs to States** – state and local governments will receive no funding from the federal government in exchange for providing this service. Additionally, states will likely have to make programming changes to financial and accounting systems, purchase new software, register vendors, possibly hire additional staff, and keep massive new data files and paper reports.

- Applies only to public sector – state and local governments would be required to withhold three percent on payments, but private companies would not. This could place state and local governments at a disadvantage.
- Lack of consultation – neither the original House nor Senate version of the *Tax Increase and Prevention Act of 2005* contained the withholding requirement. Instead, the provision was added in the conference committee. This prevented state and local governments from expressing their views on the measure.
- Perceived need for withholding arose regarding federal contracts – one of the main justifications for the withholding provision is that the Government Accountability Office (GAO) issued a report showing that 3,800 General Services Administration (GSA) federal contractors had tax debts. Instead of creating a withholding provision that applies to all levels of government, Congress could have passed a law that only applies to federal contractors.
- Inflating bids – vendors and contractors could increase their bids by three percent in order to compensate for withholding. This would cause state and local governments to spend additional funds.
- Purchasing cards – the provision also requires withholding on purchases made by purchasing cards. Many questions have been raised regarding how withholding can be accomplished using purchasing cards.
- Many unanswered questions – in addition to the other issues, many additional unanswered questions remain regarding withholding, including how to report withheld amounts to the IRS or payees, how payments must be sent, and who is exempt and who is not.

### **CURRENT STATUS OF WITHHOLDING PROVISION**

Shortly after the *Tax Increase Prevention and Reconciliation Act of 2005* was signed into law this past May, Senator Larry Craig (R-Idaho) introduced legislation calling for the repeal of the withholding provision. Sen. Craig stated that, "Proponents of the withholding provision describe it as closing a loophole. That is nonsense. Reporting requirements are already in place for government contractors. All this does is buck the IRS's collection responsibilities to the taxpayers." In addition to Sen. Craig's legislation, Congressman Wally Herger (R-California) has also introduced legislation calling for repeal.

Furthermore, the National Association of Counties (NACo) has called for the repeal of the withholding requirement on the grounds that it is an unfunded mandate. Other state and local associations are continuing to monitor the issue and are hopeful that if the provision is not fully repealed, the Department of Treasury will take their concerns into consideration when establishing rules and guidelines.

*If you would like additional information regarding the government withholding provision, please contact Brian Sigriz at (202) 624-8439 ([bsigriz@nasbo.org](mailto:bsigriz@nasbo.org)) or Scott Pattison at (202) 624-8804 ([spattison@nasbo.org](mailto:spattison@nasbo.org)) in NASBO's Washington D.C. office.*

# United States Senate

WASHINGTON, DC 20510

June 12, 2007

The Honorable Max Baucus, Chairman  
The Honorable Charles E. Grassley, Ranking Member  
Committee on Finance  
United States Senate  
219 Dirksen Senate Office Building  
Washington, DC 20510

Dear Chairman Baucus and Ranking Member Grassley:

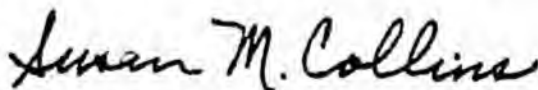
We write to you regarding the new 3% withholding tax on federal, state, and local government contracts for goods and services enacted as Section 511 of the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222). This 3% withholding tax is scheduled to go into effect in 2011.

While we understand and support your commitment to closing the tax gap, we do not believe that Section 511 is the appropriate means to achieve that goal. We are concerned that the 3% withholding provision is overbroad, and will unfairly penalize contractors that pay their taxes. Many of these contractors operate on very narrow profit margins – often 3% or less – and will be unable to comply with Section 511's withholding requirement without sacrificing the lion's share of their cash flow.

We are particularly concerned about the impact of the 3% withholding provision on small businesses in the construction industry. Contractors rely on their cash flow to finance investment and expansion, and as security for bonds they are required to hold in order to do business with the federal government. The 3% withholding requirement may so severely restrict cash flow that contractors will find it difficult or impossible to secure bond coverage, and as a result, many contractors will be driven out of the market. This, in turn, will lead to higher prices for the goods and services they supply to the federal government.

We are seeking a workable alternative to Section 511 that helps to address the problem of the tax gap without placing an undue burden on honest contractors. We would welcome the opportunity to work with you towards that end.

Sincerely,



SUSAN M. COLLINS  
United States Senator



NORM COLEMAN  
United States Senator

# United States Senate

WASHINGTON, DC 20510

June 12, 2007

The Honorable Max Baucus, Chairman  
The Honorable Charles E. Grassley, Ranking Member  
Committee on Finance  
United States Senate  
219 Dirksen Senate Office Building  
Washington, DC 20510

Dear Chairman Baucus and Ranking Member Grassley:

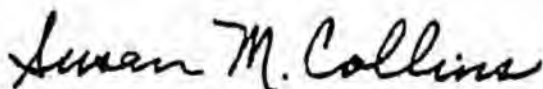
We write to you regarding the new 3% withholding tax on federal, state, and local government contracts for goods and services enacted as Section 511 of the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222). This 3% withholding tax is scheduled to go into effect in 2011.

While we understand and support your commitment to closing the tax gap, we do not believe that Section 511 is the appropriate means to achieve that goal. We are concerned that the 3% withholding provision is overbroad, and will unfairly penalize contractors that pay their taxes. Many of these contractors operate on very narrow profit margins – often 3% or less – and will be unable to comply with Section 511's withholding requirement without sacrificing the lion's share of their cash flow.

We are particularly concerned about the impact of the 3% withholding provision on small businesses in the construction industry. Contractors rely on their cash flow to finance investment and expansion, and as security for bonds they are required to hold in order to do business with the federal government. The 3% withholding requirement may so severely restrict cash flow that contractors will find it difficult or impossible to secure bond coverage, and as a result, many contractors will be driven out of the market. This, in turn, will lead to higher prices for the goods and services they supply to the federal government.

We are seeking a workable alternative to Section 511 that helps to address the problem of the tax gap without placing an undue burden on honest contractors. We would welcome the opportunity to work with you towards that end.

Sincerely,



SUSAN M. COLLINS  
United States Senator



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United States Senator