



Opening Statement

Chairman Mick Mulvaney

House Subcommittee on Contracting and Workforce

Hearing Entitled: Defer No More: The Need to Repeal the 3% Withholding Provision

May 26, 2011

I am pleased to spend my first hearing as Chairman of this subcommittee focusing on a government policy that is such a bad idea that when it was first enacted in 2006, Congress immediately delayed its implementation for five years until 2011. And when 2011 rolled around, Congress again delayed implementation of the 3% withholding requirement for another year. Now, the IRS is causing further delays of the withholding requirement until 2013 because, they say, implementation would be too difficult – even though they’ve had six years to prepare. Well, since no one seems interested in implementing this policy, hopefully this hearing can build on this Congress’s successful bipartisan repeal of the onerous 1099 reporting requirements and serve as the starting point for congressional action to repeal it.

The original intent of this 3% withholding requirement was to close the “tax gap.” In other words, 3% withholding was supposed to reduce the amount of taxes that were owed but went unpaid. Similarly, the enhanced 1099 reporting requirements discussed in the Small Business Committee and repealed through bipartisan efforts in the House and Senate also sought to close the “tax gap.” Both enhanced 1099 reporting and 3% withholding requirements sought to close the tax gap through increased burdens on businesses of all types, but small businesses will be hurt the most.

Small businesses today already operate on thin profit margins with little room for any additional withholding. As has been discussed in the Small Business Committee several times already this year, regulatory burdens fall particularly hard on small businesses and the 3% withholding requirement is no exception. Many small business contractors, including those testifying today, work for the government for less than a 3% profit margin. This 3% withholding requirement would force these contractors to wait until the end of the tax year to fully recoup

their expenses, much less take home any profit. Also troubling is the possibility that government contractors will not have the funds to pay their subcontractors during a project and will then have to find an outside source of financing simply to complete the contract. Nobody here needs a reminder of the difficulties small businesses currently face in obtaining credit.

Even worse is the fact that implementing this 3% withholding requirement means treating all small business contractors with suspicion. Instead of rewarding those small businesses that choose to compete for and win contracts, the government essentially pre-accuses them of cheating on their taxes and withholds 3% of all payments. The government already requires all contractors to certify that they are in compliance with federal tax law. So, why should we assume that they will break the law when they win a contract?

At a time when state and local governments are struggling along with citizens everywhere to recover from the recent recession, the 3% withholding requirement represents an expensive unfunded mandate that will further strain state and local government finances. I look forward to hearing the testimony of the Treasurer from my home state of South Carolina on the devastating effects of this requirement.

We also have witnesses from the Defense Department with us today to testify as to the great expense that this 3% withholding requirement will impose and how these expenses far exceed any projections for additional tax revenue produced. It makes no sense for DOD to spend \$17 billion over five years in order to save less than \$6 billion in the first year and only \$200 million a year thereafter.

The Joint Committee on Taxation predicted that after the first year, all increases in tax revenue from this 3% withholding requirement will come from interest the government will earn on the withheld money. In essence, the government will be forcing small businesses to loan the government money. I look forward to hearing from the small businesses that will testify today as to all the other ways this 3% withholding requirement will affect them.