

## **Statement of Rep. Wally Herger (CA-2)**

### **Hearing on the Need to Repeal the 3% Withholding Provision**

#### **House Committee on Small Business Subcommittee on Contracting and Workforce**

**May 26,2011**

Chairman Mulvaney, Ranking Member Chu, and Members of the Subcommittee – Thank you for holding this hearing on the need to repeal the 3% withholding tax on government contracts. As someone who has been passionately opposed to this tax from the day it was first signed into law, I am encouraged by the Committee’s interest in this issue.

Section 511 of the Tax Increase Prevention and Reconciliation Act of 2005 requires government agencies at all levels – federal, state, and local – to withhold 3 percent of payments for goods and services, effective in 2012. The Internal Revenue Service has recently issued regulations delaying this requirement until January 1, 2013, but agencies and businesses must still plan for it to eventually take effect. The breadth of this 3% withholding tax is truly astounding. It affects everyone from the manufacturer who builds tanks for the Army to the nursing home that cares for poor seniors on Medicaid, from the

construction workers who repair roads and levees to the commissaries that sell groceries to families on military bases.

As the members of this Subcommittee are well aware, small businesses are the lifeblood of our economy. I come from a small business background myself, so I have firsthand knowledge of how our country's entrepreneurs and job creators are burdened by a complex tax code and cumbersome regulations. If the 3% withholding tax is permitted to go into effect, it will only add to that burden. Many businesses that contract with the government operate on very narrow profit margins – often less than 3 percent. As a result, this tax will create serious cash flow problems for small businesses.

Today, our economy is in poor condition. The stock market may have improved from the low point of the recession, but for most Americans, the signs of recovery have been few and far between. Millions of people are still without work. In my northern California congressional district, some counties have more than 20% unemployment. Government regulations and taxes that were a bad idea even in happier times, are absolutely disastrous when our economy is struggling to recover and create jobs.

In addition to its impact on small businesses, the recession has also taken a toll on state and local government finances. Cities, counties, and states across America are struggling to balance the

budget without raising taxes or slashing vital services. The 3% withholding tax would worsen this fiscal crisis by creating new administrative costs and potentially raising procurement costs for state and local governments.

Supporters of the 3% withholding requirement have billed it as a tax compliance measure. Yes, it's a problem when government contractors don't pay their taxes. But instead of slapping a new tax on everyone – a tax that will actually cost the government more to collect than it raises in revenue – we could simply stop awarding government contracts to people who cheat on their taxes. In fact, since the 3% withholding provision became law, OMB and the Treasury Department have announced several initiatives to do just that. Hopefully these new compliance measures will provide the final push for Congress to repeal 3% withholding once and for all.

Again, I appreciate the opportunity to testify this morning, and I look forward to working with the Chairman and other members of this committee to move ahead with repeal.