Portfolio Analysis:

Report on the Federal Government's Delinquent Non-Tax Debt

Part I: Overview

In 1996, Congress passed the Debt Collection Improvement Act (DCIA) delegating significant responsibility to the Department of the Treasury to maximize the collection of non-tax delinquent debt owed to the Federal government. The DCIA specifically mandates that Federal agencies, with certain exemptions, transfer non-tax debt over 180 days delinquent to the Department of Treasury for collection.

The DCIA authorizes two key tools for collection of referred delinquent debt -- centralized administrative offset and government-wide cross-servicing. In administrative offset, Treasury has developed a process to match Federal payments against debts owed to the Government. When a match occurs, the payment is intercepted and the debt is offset up to the amount of the debt. Collections made through this process are returned to the Federal agency that is owed the debt, less a pre-determined fee to cover operational expenses. The other tool available is government-wide cross-servicing. Government-wide cross-servicing requires Federal agencies to refer debts delinquent over 180 days to Treasury for centralized collection efforts. FMS is managing this process and utilizes a variety of collection tools and strategies, including private collection agencies, demand letters, administrative offset and negotiated repayment agreements.

At the end of Fiscal Year 1997, the Federal Government reported over $ 1 trillion in outstanding non-tax receivables and guaranteed loans. According to the Department of the Treasury, $51.9 billion or approximately 5 percent of that was delinquent. The DCIA authorizes Treasury to collect the portion of government-wide debt that is over 180 days delinquent. The Financial Management Service (FMS) requested that Price Waterhouse assist it in estimating the amount referable to and collectible by Treasury.

Part II: Breakdown of the $51.9 billion

Table 1, on the following page, presents a summary of delinquent debt. This table shows that the total delinquent debt is $51.9 billion. Of this amount, $4.7 billion is not required to be transferred to Treasury because it is less than 180 days delinquent. Of the remaining $47.2 billion, $18.2 billion is ineligible for transfer to Treasury because of the following exemptions under the DCIA:

- the borrower has declared bankruptcy[1]
- the debt is owed by a foreign government[2]
- the debt is in forbearance or appeals[3]
- the debt is in foreclosure[4]

[1] The automatic stay mandated by 11 U.S.D. 362 generally prevents the government from pursuing collection against debtors in bankruptcy.
[2] Debts owed by foreign governments.
[3] Debts that are subject to forbearance or that are not generally "legally enforceable." The government cannot pursue collection against a debt, if it is not legally enforceable. Most credit-granting agencies are subject to forbearance requirements by statute and/or regulation.
[4] Foreclosure is governed by State law. In some States (such as California and Idaho), to maintain the right to foreclose, a creditor must foreclose the collateral securing the debt before seeking other collection remedies. In these States, offsetting payments could preclude the government from pursuing foreclosure.

Table 1 - Summary Analysis of Delinquent Debt
Total Government (as of September 30, 1997)

	Estimated Delinquent Debt ($ in Million)
Total Government	**$51,902**
Less Than 180 Days	$4,728
Delinquent Debt Over 180 Days [5]	**$47,174**
Debt Excluded from Offset	
In Bankruptcy [6]	($3,381)
Foreign Debt [7]	($3,917)
Forbearance or In Appeals [8]	($6,381)
In Foreclosure [9]	($3,571)
Other (Accelerated Debt not Due) [10]	($875)
Subtotal	**($18,125)**
Eligible to Refer to Treasury for offset	**$29,049**
Debt Excluded from Cross-Servicing [11]	
At Private Collection Agents	($5,937)
At DOJ	($3,857)
Eligible for Internal Offset	($712)
At Third Party	($10,448)
Other [12]	$436
Subtotal	**($20,518)**
Eligible to Refer to Treasury for Cross Servicing	**$8,531**

5 The Revised Report on Receivables indicates $47,174 million in deliquent debt over 180 days.

6 The automatic stay mandated by 11 U.S.D. 362 generally prevents the government from pursuing collection against debtors in bankruptcy.

7 Debt owed by foreign governments.

8 Debts that are subject to forbearance or that are not generally "legally enforceable." The government cannot pursue collection against a debt, if it is not legally enforceable. Most credit-granting agencies are subject to forebearance requirements by statute and/or regulation.

9 Foreclosure is governed by State law. In some States (such as California and Idaho), to maintain the right to foreclose, a creditor must foreclose the collateral securing the debt before seeking other collection remedies. In these States, offsetting payments could preclude the goverment from pursuing foreclosure.

10 Other includes USDA accelerated debt not past due, and VA erronuous reporting.

11 Debts that are excluded for offset are also excluded for cross-servicing for the same reasons stated in Notes 2 through 4 and Note 6. The DCIA exempts debts in foreclosure for referral to Treasury for cross-servicing.

12 Adjusted to include $436 million in non-judicial foreclosure deficiencies for VA that can not be collected by offset by statute.

After the exclusions are subtracted, the remaining $29.0 billion is eligible to be transferred to Treasury for offset. This amount is further reduced to determine the amount which is also available for cross-servicing. Debts are excluded from cross-servicing for the following reasons:

- the debt is at a private collection agency
- the debt is at the Department of Justice for litigation
- the debt is eligible for internal offset
- the debt is at a third party for collection (Education debt at the guarantee agencies)
- the debt is at a Debt Collection Center that has been approved by Treasury
- the Agency has an approved asset sale program

Once these exclusions are included, the amount eligible for cross-servicing is $8.5 billion. These debts in cross-servicing are also available for offset, i.e. debts available for cross-servicing are a subset of the debts available for offset.

The following sections discuss the collectibility of this debt through the administrative offset and cross servicing programs.

Part III: Collectible from Offset

As previously stated, the DCIA mandates, among other things, that Treasury develop a centralized process to match Federal payments against debts owed to the Government. When a match occurs and a payment recipient who also owes a Federal debt is identified, the payment is reduced or offset, by the amount of the debt or payment, whichever is less (with some restrictions). Payments that can be matched under this program include benefit payments made under the Social Security Act (SSA), certain programs under Railroad Retirement and Black Lung, vendor miscellaneous payments, Office of Personnel Management (OPM) retirement, Federal salary and Federal tax refund payments.

While the concept is a simple one, the amount of debt that can be collected through administrative offset is limited by a number of complex factors including the offset provisions set forth in the DCIA and the likelihood that recipients of the Federal payments subject to offset will also be delinquent debtors. For example, while 100 percent of tax refund payments may be offset to satisfy delinquent Federal debts, the DCIA limits offset of Federal salary payments to 15 percent of disposable pay, and most benefit payments are subject to a $9,000 annual exemption before any offsets can take place. Furthermore, in tests run by FMS to determine the likelihood of various types of offsets, it was estimated that less than 0.34 percent of all salary payments and 0.08 percent of SSA benefit payments matched records in the delinquent debtor database.

In developing the estimate for collectibility through the administrative offset program, we separately evaluated each of the payment types that comprise the program. For tax refund payments, we used historical data over the past 5 years to estimate annual collections. We relied on a test conducted by the Department of the Treasury to obtain collectibility estimates for salary and Social Security benefit payments.

To estimate the Tax Refund portion of the administrative offset program, we calculated the average collections over the last 5 years. This average was used to estimate an annual collection of $661 million. It should be noted that this number does not include amounts collected for Child Support which were over $1.1 billion dollars in CY97.

Treasury has conducted tests to project how much debt could be collected once Federal salary payments are fully incorporated into administrative offset. Specifically, Treasury matched one pay period of payroll from the Department of Agriculture, National Finance Center (NFC) to the debtor database. Treasury took the results of that match and extrapolated an estimate of collections if all Federal salary payments were matched against the debtor database. By this method, between $48 million and $80 million could be collected annually through salary offset[13]. However, this type of test needs to be conducted over a longer period of time with alternative payroll sources in order to increase the reliability of this procedure.

In addition to the salary test, Treasury conducted a test matching Social Security benefit payments for one month against the debtor database. The results were extrapolated to estimate the collections expected once benefit payments are fully incorporated into administrative offset. This test concluded that between $37 million and $61 million could be collected annually[14]. This test will need to be conducted over an extended period of time to increase confidence in the results.

Table 2 presents the projected collectibility ranges for the offset programs once all payment types have been incorporated into the program.

Table 2 - Annual Estimated Range of Collectibility through the Administrative Offset Program [15] ($ in millions)

	Low	High
Tax Refund Offset (FY 1997 collection) [16]	$661	$661
Salary Offset (annual estimate)	$48	$80
Social Security Offset (annual estimate)	$37	$61
OPM & Misc. Vendor Payments	$1	$1
	$747	**$803**

[13] This does not include amounts which are projected to be collected for Child Support. Child Support is currently not participating in Treasury's salary offset. Projections were based on amounts Treasury could collect or that Treasury could cause to be collected at agency locations through repayment plans.
[14] Projections were based on amounts Treasury could collect or that Treasury could cause to be collected at agency locations through repayment plans.
[15] The variation between low and high range represents a discounting of expected collections to account for any variations in test results.
[16] This does not include collections for child support which were over $1.1 billion in CY97.

Part IV: Collectible from Cross-Servicing

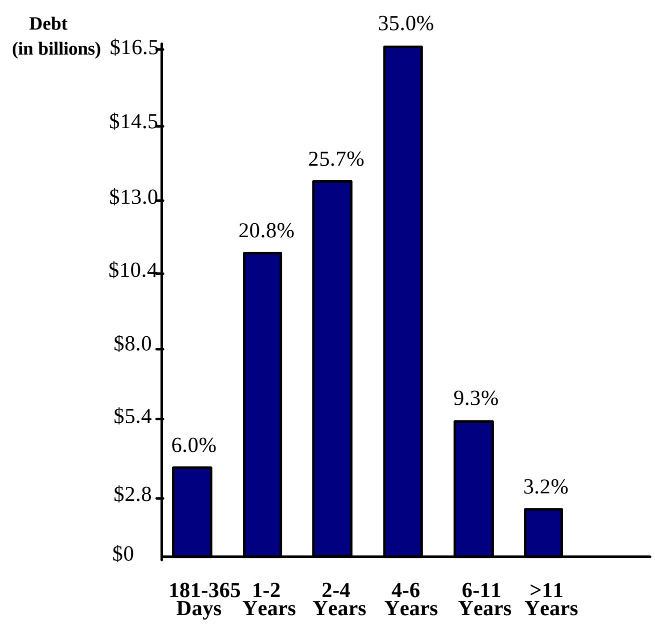
To estimate the amount collectible by Treasury through the cross-servicing program we analyzed the impact of age of the debts and private collection agency experience to the debt portfolio.

Aging Analysis

As a general rule, successful debt collection becomes increasingly difficult as delinquencies age. In analyzing the delinquent debt reported by agencies to Treasury, Price Waterhouse estimated that the bulk of this debt is between one and six years old, with a large portion falling between four and six years old. Chart 1 below depicts the age distribution of non-tax debt greater than 180 days delinquent, illustrating that only 6.0 percent is between 181 and 365 days delinquent and 12.5 percent is older than six years. Although the age distribution varies somewhat by agency, collection results consistently show that the oldest debts have very little recovery value.

Chart 1. United States Government

Percentage of Estimated Delinquent Debt Greater than 180 Days by Age



The percentages represent the breakdown of delinquent debt by age based on financial data provided by the Small Business Administration, U.S. Depts. Of Agriculture, Education, Housing and Urban Development, Treasury, and Veterans Affairs.

Private Collection Agency Experience

We interviewed two of the country's largest private sector collection agencies (PCAs) to obtain information on their collection rates stratified by the age of the debt. These rates were then used to estimate the collectibility of the debt eligible for referral to Treasury for cross-servicing. These PCAs are presently under contract with the Department of the Treasury to collect delinquent debt. Table 3 presents their collection rates by the age of the debt.

Table 3 - Private Collection Agency Experience - Recovery Rates

	Private Collection Agencies	
Age of Delinquent Debt	**Low**	**High**
Debt 181 - 365 days Delinquent	7.8%	14.0%
Debt 1 - 2 years Delinquent	2.3%	5.0%
Debt 2 - 4 years Delinquent	1.0%	1.1%
Debt 4 - 6 years Delinquent	0.4%	1.0%
Debt 6 - 11 years Delinquent	0.2%	1.0%
Debt 11+ years Delinquent	0.0%	1.0%

Cross-Servicing Collectibility

Table 4 presents our estimate of collectibility of the delinquent debt.

Table 4 - Estimate of Collectibility through Cross Servicing ($ in millions)

			Low		High	
	Age Distribution	**Debt by Age**	**Collection Rate**	**Collection Estimate**	**Collection Rate**	**Collection Estimate**
Debt 181 - 365 days Delinquent	6.0%	$515	7.8%	$40	14.0%	$72
Debt 1 - 2 years Delinquent	20.8%	$1,771	2.3%	$41	5.0%	$89
Debt 2 - 4 years Delinquent	25.7%	$2,191	1.0%	$22	1.1%	$24
Debt 4 - 6 years Delinquent	35.0%	$2,989	0.4%	$13	1.0%	$30
Debt 6 - 11 years Delinquent	9.3%	$790	0.2%	$2	1.0%	$8
Debt 11+ years Delinquent	3.2%	$275	0.0%	$0	1.0%	$3
Total Annual Collections from Cross Servicing		**$8,531**		**$117**		**$225**

We calculated these estimates by stratifying the debt by age and multiplying it by the relevant collection rates to get a low and high collection estimate. By this method, between $117 million and $225 million could be collected annually through cross-servicing

During the course of our work we learned that agencies are unlikely to immediately transfer debt to the Treasury at 180 days. This may result in an overstatement of the amount of debt falling into the 181 - 365 days category. If this is true, Treasury would be unable to collect as much of this portion of the debt as estimated.

Part V: Conclusion

Analysis of the $51.9 billion in non-tax delinquent debt owed to the Federal government reveals that $29.0 billion is eligible for referral to Treasury for offset. A portion of this amount - $8.5 billion, is also available for cross-servicing. When all payment streams are incorporated into the administrative offset program and all eligible debt is referred to Treasury, we project $864 million to $1 billion will be collectable[17] on an annual basis. Table 5 presents our estimate of debt collectible by Treasury from offset and cross-servicing.

Table 5 - Annual Range of Collectible Debt ($ in millions)

	Low	High
Administrative Offset:		
Tax Refund Offset	$661	$661
Salary Offset	$48	$80
Social Security Offset	$37	$61
OPM & Misc. Vendor Payments	$1	$1
Cross-Servicing	$117	$225
Total [18]	**$864**	**$1,028**

[17] Projected collections will need to be adjusted for Black lung, Railroad retirement, and Non-Treasury Disbursing Office vendor payments.
[18] See footnote above.