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Joint Committee on Finance

Paper #211

Interest on Child Support Arrears (Children and Families -- Child Support)

[LFB 2013-15 Budget Summary: Page 121, #3]

CURRENT LAW

Whenever a court enters a judgment of annulment, divorce, or legal separation; approves a stipulation for child support; enters an order or judgment in a paternity action or action for child or family support; or in actions to compel support or in voluntary acknowledgements of paternity, the court must direct either one or both parents to pay an amount reasonable or necessary to fulfill the parental responsibility to provide for their minor children.

When child support payments are not made according to the court order, the past-due amount, known as arrears, accrues, and interest is charged at the rate of 1% per month on any amount in arrears equal to or greater than the amount of child support due in one month.

Under the temporary assistance for needy families (TANF) program, as under the former aid to families with dependent children (AFDC) program, recipients must assign to the state the right to collect any child support obligations that come due while the family receives benefits, not to exceed the total amount of assistance provided. The state distributes the assigned child support, including arrears, as follows: (a) first pay to the federal government the federal share of the support collected; and (b) retain, or distribute to the family, the remaining amount collected. The federal share is based on the federal financial participation rate for the Medicaid program in effect during the year in which collections were made (currently about 60% in Wisconsin).

Beginning January 1, 2010, all assigned arrears are passed through to the family if the family is no longer receiving assistance. The federal Deficit Reduction Act of 2005 authorized states to pass through all arrears that accumulated while an individual received TANF assistance, if the individual was no longer receiving TANF assistance, without having to pay the federal share on these amounts.

GOVERNOR

Provide \$182,500 PR in 2013-14 and \$365,000 PR in 2014-15 to reflect an increase in revenue from assigned child support arrears paid by noncustodial parents and not passed through to the family, due to implementation of a pilot project to reduce the interest rate on child support arrears. Authorize the Department of Children and Families (DCF) to conduct a pilot project that would reduce the interest that accrues on the amounts in arrears to 0.5% per month from 1.0% under current law. Specify that if DCF conducts the pilot project, the program may begin after December 31, 2013, but must end on June 30, 2015, and that the reduced interest rate would only apply to interest that accrues during that period of time. Require the interest rate to revert to 1% per month at the end of the pilot project unless the Department of Administration (DOA) approves continuation of the lower rate. The state's share of the increase in assigned child support arrears is estimated to be \$73,000 in 2013-14 and \$146,000 in 2014-15. The remainder (estimated at \$109,500 in 2013-14 and \$219,000 in 2014-15) would be paid to the federal government.

DISCUSSION POINTS

1. The costs of administering child support enforcement activities performed by counties in Wisconsin are supported by a combination of federal funds, state general purpose revenue (GPR), and county revenue from local sales tax, property tax, and shared revenue. The largest source of funding for child support enforcement activities comes from the federal government in the form of federal child support incentive payments and federal matching funds.

2. The federal government distributes child support incentive payments to states in order to encourage and reward state programs that perform in a cost-effective and efficient manner. States must compete against each other for incentive dollars. The annual incentive payment to each state is based on that state's performance, relative to the other states, on several criteria. One of these criteria is the collection of child support arrearages. This performance measure is determined by dividing the number of Title IV-D child support cases paying towards arrears by the total number of these cases with arrears owing. Title IV-D child support cases, under Title IV-D of the federal Social Security Act, are child support cases that involve a person who has received public assistance and has been referred for child support services, or a cases that involve a person who has applied for child support services.

The Urban Institute Report

3. On July 11, 2007, the Urban Institute released a report, *Assessing Child Support Arrears in Nine Large States and the Nation*, prepared for the federal Office of Child Support Enforcement (OCSE). The purpose of the report was to provide information regarding the increasing amount of child support arrears nationwide and how to help OCSE and state child support programs to manage these arrears. The report focused on Arizona, Florida, Illinois, Michigan, New Jersey, New York, Ohio, Pennsylvania, and Texas.

4. This report stated that in September, 2006, OCSE reported \$105.4 billion in arrears

had accumulated nationwide since the program began in 1975, which represented a 10-fold increase in 19 years.

5. The report found that most of the arrears are owed by a relatively small number of non-custodial parents, each of whom owes a large amount of arrears. The report estimated that 43% of the nation's certified arrears were owed by 10% of the debtors, each of whom owed over \$40,000 in certified arrears. Nearly 75% of these high debtors had no reported income or income of \$10,000 or less per year. As a result, wage withholding is not effective among this population. It is also difficult to collect arrears from this group of people by other means.

6. The report indicated that obligors with no income owed 40% of the arrears in the states examined and estimated that only 16% of their arrears would be paid over a 10-year period. Similarly, those with incomes of \$10,000 or less owed 30% of the arrears and were estimated to pay 27% of their arrears over a 10-year period.

7. The report then focused on why arrears have grown rapidly. The primary factor has been the assessment of interest on a routine basis. The report noted that 18 states charged interest on a routine basis, including Wisconsin, 18 states charged interest but did so intermittently, and 14 states did not charge interest. The report found that between 1987 and 2006, states that charged interest routinely experienced more than a 10-fold increase in arrears. During the same time period, the other states' arrears grew half as fast.

8. The report discussed six strategies to manage existing arrears: (a) provide accurate information about arrears owed; (b) increase arrears collections; (c) revise interest policy; (d) implement arrears amnesty programs; (e) implement arrears compromise programs; and (f) review non-paying arrears cases for possible case closure.

Child Support Arrears in Wisconsin

9. In federal fiscal year (FFY) 2010, of the fifty states plus Puerto Rico, Guam, the Virgin Islands, and the District of Columbia, Wisconsin ranked 16th in establishment of support orders, 3rd in collection of current child support due, 26th in collection of child support arrearages, and 16th in cost-effectiveness. Of the states that report paternity establishment of Title IV-D cases, rather than statewide cases, Wisconsin ranked 13th.

10. In FFY 2011, of the fifty states plus Puerto Rico, Guam, the Virgin Islands, and the District of Columbia, Wisconsin ranked 23rd in establishment of support orders, 4th in collection of current child support due, 22nd in collection of child support arrearages, and 12th in cost-effectiveness. Of the states that report paternity establishment of Title IV-D cases, rather than statewide cases, Wisconsin ranked 11th.

11. In FFY 2010, Wisconsin received 100% of the amount of federal incentive funding allocated for the following performance measures: (a) paternity establishment; (b) support order establishment; and (c) cost-effectiveness. The state received 80% of its allocation for current support collections and 72% of its allocation of arrears collections. In FFY 2011, Wisconsin performed similarly, except that 73% of its allocation of arrears collections was received. The state

must have an arrears collection rate of 80% in order to receive the full allocation for this performance measure. The state's performance rate was 62.1% in FFY 2010 and 63.5% in FFY 2011.

12. Table 1 shows the amount of arrearages owed, total arrears collected, the percentage of arrears collected, and the percentage of arrearages due to interest for state fiscal year (SFY) 2007-08 through 2011-12.

TABLE 1
Arrears Owed, Arrears Collected, Percent Collected, Percent Due to Interest
2007-08 thru 2011-12
(Millions)

	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>
Arrears Owed	\$4,286.4	\$4,471.4	\$4,729.6	\$4,971.5	\$5,193.8
Arrears Paid	186.9	188.8	175.0	176.1	178.5
Percent Paid	4.4%	4.2%	3.7%	3.5%	3.4%
Percent Due to Interest	36.2%	37.9%	39.0%	40.0%	41.0%

13. Table 2 shows the amount of interest on arrears owed, the amount of interest collected, and the percentage of interest collected for SFY 2007-08 through 2011-12.

TABLE 2
Interest Owed, Interest Collected, and Percent Collected
2007-08 thru 2011-12
(Millions)

	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>
Interest Owed	\$1,553.0	\$1,692.9	\$1,843.4	\$1,986.4	\$2,127.7
Interest Paid	17.0	17.8	19.3	19.6	19.5
Percent Paid	1.1%	1.1%	1.0%	1.0%	0.9%

14. Local child support agencies monitor cases to ensure court orders are being followed. Various measures may be taken in order to collect arrears. Automatic income withholding may be implemented, which may be increased without a court action if past-due support is owed. DCF also has the authority to intercept tax refunds, deny loans, grants, or passports, or impose liens on property. DCF also may deny a license or take other court actions. In addition, child support agencies may agree to enter into a payment plan with an obligor in order to prevent some enforcement measures.

Families Forward Program

15. The Institute for Research on Poverty (IRP) at the University of Wisconsin-Madison

implemented a pilot program in Racine County to address growing child support debt in Wisconsin on behalf of DCF's Bureau of Child Support. Eligibility for the Families Forward program was limited to noncustodial parents with total child support arrearages of at least \$2,000 and a recent history of nonpayment. Enrollment began in May of 2005 and ended in November of 2007.

16. The Families Forward program had two features to address the reduction of arrears: (a) suspension of interest during program participation; and (b) arrears forgiveness for participants who made payments on current support or arrears. No interest accrued for participants during the pilot program, and the state agreed to reduce debt owed for assigned child support arrears by 50 cents for every dollar the participant paid toward current support or arrears. The same arrangement applied to family-owed arrears if the custodial parent agreed to the arrangement. Credit earned was applied to arrears quarterly, beginning with the interest balance. Participation ended if the obligor failed to make any payment in two consecutive quarters.

17. In January of 2011, IRP released its final report, *The Families Forward Program Final Evaluation Report*. The evaluation found that Families Forward program participants: (a) made larger payments toward current support and arrears; (b) were more likely to pay; (c) were more likely to pay more frequently; and (d) reduced their state-owed arrears (by \$2,700 more than non-participants) and family-owed arrears (by \$2,500 more than non-participants).

Interest on Arrears

18. The Committee could adopt the Governor's recommendation to establish a pilot project to reduce the interest rate on child support arrears from 1% per month to 0.5% per month and provide \$182,500 PR in 2013-14 and \$365,000 PR in 2014-15 to reflect an increase in revenue from assigned child support arrears paid by noncustodial parents (Alternative A1). The Urban Institute report named the routine assessment of interest on arrears as the single most important factor contributing to arrears growth during the past 15 years.

19. Prior to 2011 Wisconsin Act 69, interest on debt owed under a civil judgment was 12% annually, the same as child support arrears. Under current law, the interest rate imposed on a civil judgment debt is 1% plus the prime rate in effect on January 1 of the year in which the judgment is entered if the judgment is entered before June 30 or in effect on July 1 of the year in which the judgment is entered if the judgment is entered after June 30 of that year. Currently, 1% plus the prime rate in effect on January 1, 2013, is 4.25%.

20. Reducing the child support arrears interest rate to 0.5% per month from 1% per month would total 6% annually. This interest rate is still higher than the interest rate applied to a civil judgment debt, but is more comparable than the current 12% annual interest rate. In addition, local child support agencies currently have a variety of tools and methods to collect arrears, noted in paragraph #14 above, but those tools and methods have not been effective in increasing payments or reducing overall arrears. Lowering the interest rate on arrears may provide an incentive for noncustodial parents to make larger or more frequent payments, as shown in the Families Forward program.

21. Alternatively, the Committee could delete the provision and, compared to the bill,

reduce revenue by \$182,500 PR in 2013-14 and \$365,000 PR in 2014-15 (Alternative D1). Higher interest rates imposed on child support arrears could send a message that paying money owed to their children is a higher priority than payment of other debts in order to ensure that their children are provided for. In addition, imposition of interest on arrears may compensate custodial parents and their children for the delay in receiving child support payments.

22. On the other hand, families would not be compensated and the message of high-priority payment may be ineffective if noncustodial parents simply do not repay the arrears. The Committee could modify the Governor's proposal to eliminate all interest on arrears while the pilot project is in effect. DCF estimates that a reduction in the interest rate from 1% per month to 0.5% per month would result in a 3% increase in the amount of assigned child support arrears collected. It is reasonable to assume that eliminating the interest rate, as was done under the Families Forward pilot project, would provide a greater incentive to make larger and more frequent payments, which could result in increased assigned child support arrears collected by 5%. The Committee could provide additional revenue under this alternative of \$121,700 PR in 2013-14 and \$243,300 PR in 2014-15, compared to the bill (Alternative A2). Eliminating the interest rate on child support arrears would slow the growth of arrears and could provide additional revenue to the state. The state could perform better on the federal performance standards to earn additional federal child support incentive funds. The state's share of the total increased revenue would be \$121,800 in 2013-14 and \$243,300 in 2014-15.

Amnesty Agreements

23. Although the IRP report on the Families Forward program indicated participants were more likely to make child support payments, made larger payments, and made more frequent payments, the program's success due to elimination of the interest on arrears is unclear. In the Families Forward program, debt forgiveness was also an important element of the program. For every dollar that a participant paid in current child support or child support arrears, 50 cents of the accrued arrears was forgiven.

24. The Committee could modify the Governor's provision and require DCF to implement a similar amnesty aspect to the pilot project, but limit it to the interest that has accrued (not the actual missed child support payments). The Committee could require DCF to direct local child support agencies as part of the pilot project to reduce the interest that has accrued on arrears by 50 cents for every dollar the obligor pays in current child support or child support arrears for state-owed arrears, and to offer the same arrangement for family-owed support if the custodial parent enters into an agreement to do so, in order to encourage larger and more frequent payments (Alternative B1).

25. In support of this provision, Table 1 and Table 2 above show that most of the interest on arrears is never paid. Forgiving this debt could provide an incentive for obligors to make payments in order to have the interest debt forgiven, which would result in more money going to families.

26. It is difficult to predict how much of an incentive a lower, or no, interest rate accruing on arrears would provide compared to an amnesty program that forgives interest that has

accrued on arrears. Because the obligors would already have an incentive to pay with a lower, or no, interest rate, it is unlikely that the additional amnesty program would double the payments. It is likely, however, that more and larger payments would be made. Therefore, it is estimated that an amnesty program that forgives 50 cents on each dollar paid would provide an additional 2% in revenue from assigned child support to the state (\$121,700 in 2013-14 and \$243,300 in 2014-15). The state's share would be \$48,700 in 2013-14 and \$97,300 in 2014-15.

27. Alternatively, the Committee could implement a similar amnesty program that forgives 25 cents of interest that has accrued on arrears for every dollar spent on child support and arrears (Alternative B2). This alternative would also provide the incentive to make payments, but eliminate interest on arrears at a slower rate and hold the noncustodial parent more accountable for the debt already accrued. It is estimated that this alternative would provide an additional 1% in revenue from assigned child support to the state (\$60,800 in 2013-14 and \$121,700 in 2014-15). The state's share would be \$24,300 in 2013-14 and \$48,700 in 2014-15.

28. It should be noted that there would also be an impact on family-owed arrears. As indicated above, 43% of the nation's certified arrears were owed by 10% of the debtors. It is unknown whether these debtors would be paying state-owed arrears or family-owed arrears. In addition, under the Families Forward program, participants reduced state-owed arrears by \$200 more than family-owed arrears. Finally, some families may not be willing to agree to amnesty agreements for a variety of reasons. The Families Forward evaluation noted custodial parent participation rates were disappointing because custodial parents: (a) may have had too much difficulty obtaining information about the program; (b) may not have had current contact information for the noncustodial parent; and (c) may not want to help the noncustodial parent to lower debt. However, if it is assumed that the amount of family-owed arrears paid would increase by 1% to 5%, then the amount of payments to the families would increase between \$0.7 million and \$3.4 million in 2013-14 and between \$1.3 million and \$6.7 million in 2014-15.

Extension of Interest Rate and Amnesty Agreements Beyond Pilot Project

29. The bill would require the interest rate to revert to 1% per month at the end of the pilot project unless DOA approves continuation at the lower rate (Alternative C1). The bill would also require the pilot project to end on June 30, 2015. The Committee could approve this provision and allow DOA to have the authority to extend the interest rate of 0.5% per month after the pilot project ends.

30. However, the Committee could, instead, require the interest rate to revert to 1% per month at the end of the pilot project unless DCF submits to the Committee a request to extend the interest rate approved for the pilot project (0.5% under Alternative A1 or 0% under Alternative A2) under a 14-day passive review process (Alternative C2). If a request is submitted, the Committee could require the request to include information showing the amount of the reduction in arrears owed and the increase in the number of and the dollar amount of payments towards arrears due to the lower interest rate. If the Committee approves the request, the lower interest rate used in the pilot project could continue beyond June 30, 2015.

31. In addition, if the Committee requires DCF to direct local child support agencies to

implement amnesty agreements as part of the pilot project, the Committee could require the amnesty agreements to expire at the end of the pilot project unless DCF submits to the Committee a request to extend the amnesty agreements (50 cents forgiven under Alternative B1 or 25 cents forgiven under Alternative B2) under a 14-day passive review process (Alternative C3). If a request is submitted, the Committee could require the request to include information that shows the reduction in arrears and the increase in the number of and dollar amount of payments towards arrears due to the amnesty agreements. If the Committee approves the request, the amnesty agreements could continue beyond June 30, 2015.

ALTERNATIVES

A. Interest on Arrears

1. Approve the Governor's proposal to authorize DCF to conduct a pilot project that would modify the interest that accrues on the amounts in arrears to 0.5% per month, rather than the 1.0% under current law and provide revenue of \$182,500 PR in 2013-14 and \$365,000 PR in 2014-15 to reflect an increase in revenue from assigned child support arrears.

2. Modify the Governor's proposal to authorize DCF to eliminate interest on arrears that accrue while the pilot project is in effect and provide \$121,700 PR in 2013-14 and \$243,300 PR in 2014-15 compared to the bill.

ALT A2	Change to Bill Funding
PR	\$365,000

B. Amnesty Agreements

1. In addition to Alternative A1 or A2, require DCF to direct local child support agencies as part of the pilot project to reduce the interest that has accrued on arrears by 50 cents for every dollar the obligor pays in current child support or child support arrears for state-owed arrears, and to offer the same arrangement for family-owed support if the custodial parent enters into an agreement to do so. Compared to the bill provide \$121,700 PR in 2013-14 and \$243,300 PR in 2014-15.

ALT B1	Change to Bill Funding
PR	\$365,000

2. In addition to Alternative A1 or A2, require DCF to direct local child support agencies as part of the pilot project to reduce the interest that has accrued on arrears by 25 cents for every dollar the obligor pays in current child support or child support arrears for state-owed arrears,

and to offer the same arrangement for family-owed support if the custodial parent enters into an agreement to do so. Compared to the bill provide \$60,800 PR in 2013-14 and \$121,700 PR in 2014-15.

ALT B2	Change to Bill Funding
PR	\$182,500

C. Extend Pilot Project Interest Rate or Amnesty Agreements

1. In addition to Alternative A1 or A2, approve the Governor's proposal to require the interest rate to revert to 1% per month at the end of the pilot project unless DOA approves continuation of the lower rate.

2. In addition to Alternative A1 or A2, modify the Governor's proposal to require the interest rate to revert to 1% per month at the end of the pilot project unless DCF submits to the Committee a request to extend the interest rate approved for the pilot project under a 14-day passive review process. If a request is submitted, require the request to include information showing the amount of the reduction in arrears owed and the increase in the number of and the dollar amount of payments towards arrears due to the lower interest rate. Authorize the lower interest rate used in the pilot project to continue beyond June 30, 2015, if the Committee approves the request.

3. In addition to Alternative B1 or B2, require the amnesty agreements to expire at the end of the pilot project unless DCF submits to the Committee a request to extend the amnesty agreements under a 14-day passive review process. If a request is submitted, require the request to include information that shows the reduction in arrears and the increase in the number of and dollar amount of payments towards arrears due to the amnesty agreements. Authorize the amnesty agreements to continue beyond June 30, 2015, if the Committee approves the request.

D. Delete Provision

1. Delete provision. Compared to the bill, reduce funding by \$182,500 in 2013-14 and \$365,000 in 2014-15 to reflect less revenue that would be collected from assigned child support arrears.

ALT D1	Change to Bill Funding
PR	-\$547,500

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