TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Affordable Care Act: Assessment of Internal Revenue Service Preparation for Processing Premium Tax Credit Claims

May 11, 2015

Reference Number: 2015-43-043

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

Redaction Legend:
2 = Risk Circumvention of Agency Regulation or Statute

Phone Number / 202-622-6500
E-mail Address / TIGTACommunications@tigta.treas.gov
Website / http://www.treasury.gov/tigta

AFFORDABLE CARE ACT: ASSESSMENT OF INTERNAL REVENUE SERVICE PREPARATION FOR PROCESSING PREMIUM TAX CREDIT CLAIMS

Highlights

Final Report issued on May 11, 2015

Highlights of Reference Number: 2015-43-043 to the Internal Revenue Service Director, Affordable Care Act Office.

IMPACT ON TAXPAYERS

The Patient Protection and Affordable Care Act created a refundable tax credit, referred to as the Premium Tax Credit (PTC), to assist individuals with the cost of their health insurance premiums. Individuals may elect to receive the PTC in advance as partial payment for their monthly premiums (referred to as the Advance Premium Tax Credit (APTC)) or receive the PTC as a lump sum credit on their annual Federal income tax return. Beginning in January 2015, individuals are required to reconcile the APTC and can claim additional PTC on their annual tax return beginning with Tax Year 2014.

WHY TIGTA DID THE AUDIT

This audit was initiated as part of TIGTA's continued coverage of the IRS's implementation of key Affordable Care Act tax provisions. The overall objective of this review was to assess the status of the IRS's preparations for verifying the accuracy of PTC claims during the 2015 Filing Season.

WHAT TIGTA FOUND

The IRS did not receive all required enrollment data from the Exchanges prior to the January 20, 2015, start of the 2015 Filing Season. For example, the Centers for Medicare and Medicaid Services indicated that it would not send approximately 1.7 million (40 percent) of the approximately 4.2 million Federal Exchange enrollment records to the IRS until mid-February. In addition, six of the 15 State Exchanges (including the District of Columbia) had not provided enrollment data to the IRS as of January 20, 2015. The IRS indicated that data from four of the six State Exchanges would be provided in mid-February but could not provide a time frame for when the remaining two State Exchanges would provide the required enrollment data.

In response to the delays in receiving required Exchange Periodic Data submissions, the IRS developed contingency plans in an effort to improve its ability to ensure the accuracy of PTC claims. However, without the required enrollment data from the Exchanges, the IRS will be unable to ensure that all taxpayers claiming the PTC bought insurance through an Exchange as required.

In addition, TIGTA's review of the Internal Revenue Code and the Department of Health and Human Services regulations found that the guidance does not fully address repayment of the APTC received during the months in which an enrollment inconsistency is being resolved if the individual is ultimately determined to not qualify for insurance through the Exchange. Such individuals are not entitled to the PTC. Furthermore, procedures have not been established for the Exchanges to notify the IRS when an individual is determined to be ineligible subsequent to enrollment.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS revise computer programming business requirements to use Forms 1095-A, *Health Insurance Marketplace Statement*, in conjunction with monthly data provided by the Exchanges to verify claims for the PTC. In addition, the IRS should work with the Exchanges to establish procedures to ensure that the IRS receives notification when an individual is determined to be ineligible subsequent to enrollment.

The IRS did not agree to revise computer programming to use Forms 1095-A in conjunction with monthly data and partially agreed to work with the Exchanges to identify individuals who are found to be ineligible to use the Exchange. TIGTA's concerns with the IRS's responses to the recommendations are noted in the report.

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

May 11, 2015

MEMORANDUM FOR DIRECTOR, AFFORDABLE CARE ACT OFFICE

for

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Affordable Care Act: Assessment of Internal Revenue Service Preparation for Processing Premium Tax Credit Claims (Audit # 201440325)

This report presents the results of our review to assess the status of the Internal Revenue Service's preparations for verifying the accuracy of Premium Tax Credit claims during the 2015 Filing Season. The audit is included in our Fiscal Year 2015 Annual Audit Plan and addresses the major management challenge of Implementing the Affordable Care Act and Other Tax Law Changes.

Management's complete response to the draft report is included as Appendix VI.

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. If you have any questions, please contact me or Russell P. Martin, Acting Assistant Inspector General for Audit (Returns Processing and Account Services).

Table of Contents

Abbreviations

ACA	Affordable Care Act
APTC	Advance Premium Tax Credit
CMS	Centers for Medicare and Medicaid Services
EPD	Exchange Periodic Data
FPL	Federal Poverty Line
HHS	Department of Health and Human Services
IRS	Internal Revenue Service
MEC	Minimum Essential Coverage
PTC	Premium Tax Credit
QHP	Qualified Health Plan
SLCSP	Second Lowest Cost Silver Plan

Background

The Patient Protection and Affordable Care Act (ACA)[1] created the Health Insurance Marketplace, also known as the Exchange. The Exchange is where individuals find information about health insurance options, purchase qualified health plans, and, if eligible, obtain help paying premiums. The ACA also created a new refundable tax credit,[2] the Premium Tax Credit (PTC), to assist eligible taxpayers with paying their health insurance premiums.

When enrolling in a Qualified Health Plan (QHP)[3] through the Exchange, eligible individuals can choose to have some or all of the PTC paid in advance to their insurance company as payment of their monthly premium (hereafter referred to as the Advance Premium Tax Credit (APTC)) or can wait to claim all of the PTC on their tax return. Individuals began using the Exchanges on October 1, 2013, to purchase health insurance for Calendar Year 2014. Figure 1 lists eligibility requirements to purchase insurance through an Exchange and to qualify for the PTC.

---

[1] Pub. L. No. 111-148, 124 Stat. 119 (2010) (codified as amended in scattered sections of the U.S. Code), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029.
[2] Refundable tax credits can be used to reduce a taxpayer's tax liability to zero. Any excess of the credit beyond the tax liability can be refunded to the taxpayer.
[3] A QHP is an insurance plan that is certified by the Health Insurance Exchange and provides essential health benefits, follows established limits on cost-sharing (like deductibles, copayments, and out-of-pocket maximum amounts), and meets other requirements.

Figure 1: Eligibility Requirements to Purchase Insurance Through an Exchange and Qualify for the PTC

Exchange Eligibility Requirements	PTC Eligibility Requirements
Individuals must: • Live in the United States. • Be a U.S. citizen or national or be lawfully present. • Not be currently incarcerated.	**Individuals must:** • Buy health insurance through the Exchange. • Be ineligible for insurance through an employer or government plan. • Be within certain income limits.[4] • File a joint tax return, if married. • Not be claimed as a dependent on another tax return.

Source: IRS.gov and Healthcare.gov.

Health Insurance Exchange eligibility and enrollment process

The Centers for Medicare and Medicaid Services (CMS) oversees implementation of certain ACA provisions related to the Exchanges. The CMS operates the Federal Exchange and works with States to establish State and State-partnership Exchanges, including overseeing their operations. During the Calendar Year 2014 health insurance enrollment period, 15 States (including the District of Columbia), operated their own Exchanges while the remaining 36 States partnered with the Federal Exchange. The Exchanges have sole responsibility for determining if an individual is eligible to purchase health insurance through the Exchange as well as determining the amount of the APTC they are eligible to receive. The Exchanges use a combination of Federal and State data sources to determine eligibility. The following Federal agencies provide information to the Exchanges during the enrollment and APTC eligibility process:

- The U.S. Social Security Administration verifies the applicant's Social Security Number, citizenship, wage data, and incarceration status.
- The U.S. Department of Homeland Security verifies the applicant's legal immigration status and lawful presence in the United States.

[4] The taxpayer's income must be at least 100 percent but not more than 400 percent of the Federal Poverty Line for the taxpayer's family size. For example, in Calendar Year 2013, this equated to $23,550 to $94,200 for a family of four.

- The Internal Revenue Service (IRS) provides tax return information for applicants and their family members. For example, the Exchange will use Calendar Year 2013 tax information received from the IRS in conjunction with other income data to verify an individual's estimated Calendar Year 2015 income. The Exchange uses an individual's estimated income and family status to determine if an individual is eligible to receive an APTC.

The Exchanges can also request that the IRS provide the maximum monthly APTC an individual is entitled to receive based on his or her estimated income and family size for the upcoming tax year. However, the ACA does not require the Exchanges to use the information the IRS provides when ultimately determining the amount of the APTC an individual is entitled to receive. As a result, some Exchanges created their own APTC calculator to compute this amount.

Once the Exchange determines the amount of the APTC an individual is entitled to receive, an individual then elects the actual amount to be sent to his or her insurance provider (hereafter referred to as insurer) on a monthly basis. Individuals can elect to send all, a portion, or none of the APTC to which they are entitled. Once an individual selects his or her insurance coverage and determines the amount of the APTC to be sent to the insurer, the insurer submits the information to the CMS, which then sends a request to the U.S. Department of the Treasury Bureau of the Fiscal Service to issue monthly APTC payments to the individual's insurer. According to the IRS, almost $11 billion in the APTCs was paid to insurers in Fiscal Year 2014.

Reconciliation of APTC amounts received and PTC claims

The IRS is responsible for determining the amount of the PTC a taxpayer is entitled to receive. The ACA requires all individuals for which APTC payments were made to an insurer to file a tax return to reconcile the APTC with the actual PTC they are entitled to receive based on the income and family size reported on their tax return. This reconciliation is necessary as the Exchange's computation of the APTC is based on estimates of an individual's anticipated income and family size for the upcoming calendar year. The actual amount of the PTC that taxpayers are entitled to receive is based on their actual income and family size reported on their annual tax return, which can be different from the estimates used by the Exchange to determine the allowable APTC.

Beginning in January 2015, taxpayers who purchased insurance through an Exchange are required to include Form 8962, *Premium Tax Credit (PTC)*, with their tax return to claim the PTC and reconcile any APTC payments that were made to an insurer on their behalf. Taxpayers who are entitled to more PTC than was received in advance receive the additional credit as a refund on their tax return. However, taxpayers who received more PTC in advanced payments than they were entitled to must repay the excess, subject to certain limitations, when filing their tax return. For those individuals who are assessed additional tax resulting from an overpayment, the ACA limits the amount of tax that individuals with income between 100 percent and

400 percent of the Federal Poverty Line (FPL)[5] will have to repay. However, individuals whose actual income exceeds 400 percent of the FPL are not eligible to receive the PTC and are required to repay the full amount of any APTC they received. Figure 2 lists the repayment limits for individuals with household income less than 400 percent of the FPL.

Figure 2: Limit on Repayment – Individuals Receiving Excess APTC

Household Income Percentage of the FPL	Repayment Limit – Filing Status Single	Repayment Limit – Filing Status Other Than Single
• Less Than 200%	$300	$600
• 200% but Less Than 300%	$750	$1,500
• 300% but Less Than 400%	$1,250	$2,500
• 400% or More	No Limit	No Limit

Source: Treasury Regulation Section (§) 1.36B-4.

The Exchange Periodic Data (EPD) and health insurance statements

The ACA requires the Exchanges to provide the IRS with information regarding individuals who are enrolled by the Exchange on a monthly basis. These data are referred to as the EPD. In addition, the Exchange is also required to provide an annual summary to both the IRS and the individual detailing specific information relating to the individual's enrollment. This is referred to as Form 1095-A, *Health Insurance Marketplace Statement*. The data provided by Exchanges monthly and annually include:

- Individuals and families enrolled in a QHP through the Exchange.
- Coverage start and end dates of the QHP.
- The monthly premium amount of the QHP.
- Amount of the APTCs paid for coverage under the QHP.
- Employer-offered minimum essential coverage (MEC).

As early as 2011, the IRS began developing computer programming to use the EPD at the time tax returns with claims for the PTC are processed to primarily verify that:

- The individual purchased insurance through an Exchange.

[5] The FPL is a measure of income level issued annually by the Department of Health and Human Services. The FPL is used to determine eligibility for certain programs and benefits.

- The amount of the APTC the individual received during the year is accurately reported on his or her tax return.

The ACA also requires employers and insurers to provide individuals with information related to health insurance coverage obtained outside of the Exchange. Individuals will receive a Form 1095-B, *Health Coverage*, or Form 1095-C, *Employer-Provided Health Insurance Offer and Coverage*, when they obtain insurance from a source other than an Exchange. Employers and insurers are also required to provide the Forms 1095 to the IRS. The Forms 1095 will show whether individuals were offered qualifying insurance, the individuals enrolled in health insurance coverage for the calendar year, the level of coverage, and the months for which coverage was provided. In addition, the IRS can use the Forms 1095-B and 1095-C to verify that taxpayers receiving the PTC were not eligible for insurance from their employer.

This review was performed at the IRS Headquarters in Washington, D.C., in the Affordable Care Act Office and the Affordable Care Act Program Management Office within the IRS Chief Technology Office in New Carrollton, Maryland. We also obtained information from the IRS Wage and Investment Division in Atlanta, Georgia. In addition, we obtained information from the Federal Exchange and 14 of the 15 State Exchanges.[6] This audit was conducted during the period of May 2014 through January 2015. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

[6] See Appendix IV for a list of the Exchanges.

Results of Review

Delays in Receiving Exchange Periodic Data Increase the Risk of Not Detecting Erroneous Premium Tax Credit Claims at the Time Tax Returns Are Processed

The IRS did not receive all required EPD submissions from the Exchanges prior to the January 20, 2015, start of the 2015 Filing Season. For example, the CMS indicated that it would not send approximately 1.7 million (40 percent) of the approximately 4.2 million Federal Exchange enrollment records to the IRS until mid-February.[7] In addition, six of the 15 State Exchanges had not provided enrollment data to the IRS as of January 20, 2015. The IRS indicated that data from four of the six State Exchanges would be provided in mid-February. However, the IRS has not received any indication from the remaining two State Exchanges as to when they will provide the required enrollment data. According to the IRS, it expects to continue to receive and rely on EPD submissions received after the start of the 2015 Filing Season.

Internal Revenue Code § 36B(f)(3) requires the Federal Exchange and State Exchanges to report EPD information to the IRS. Treasury Regulation § 1.36B–5, issued May 7, 2014, requires this information to be reported both monthly (by the 15th of each month) as well as annually (by January 31) to the IRS. The IRS anticipated the first EPD submission would be in June 2014 and would cover the period January 2014 through May 2014. However, the first EPD submission from an Exchange was not received until October 2014, and it contained information for only two States.

IRS management indicated that delays in the Exchanges' testing of the EPD to ensure that it conformed with CMS and IRS transmission requirements contributed to the IRS not timely receiving the required EPD. This testing helps to ensure that EPD submissions meet format and other requirements and that the Exchanges, CMS, and IRS information systems can communicate to transmit data from one system to another before the data are needed for the filing season. However, the IRS did not require the Exchanges to complete IRS testing before it would accept the EPD from the Exchanges. Regardless of whether an Exchange tested its EPD submissions with the IRS, the IRS still needs to perform checks and verifications to ensure that the data received are reliable before using it to verify PTC claims at the time tax returns are processed.

[7] As of January 20, 2015, the IRS had received partial data for individuals in 35 of the 36 States participating in the Federal Exchange.

In addition, management indicated that delays in the receipt of the EPD also result from the effectuation process in which the Exchanges reconcile enrollment records with insurer policy records. This reconciliation is necessary to ensure that data for individuals who enrolled through the Exchange and paid their premiums to maintain active health care coverage were accurately reported to the IRS.

In response to the delays in receiving required EPD submissions, the IRS developed contingency plans in an effort to improve its ability to ensure the accuracy of PTC claims. These plans include a combination of at-filing (*i.e.*, when tax returns are processed) data filters and post-processing compliance activities to address those claims that cannot be verified using the EPD. However, despite efforts to mitigate the risk of issuing improper PTC payments without the EPD, the IRS will be unable to ensure that all taxpayers claiming the PTC enrolled in a QHP through an Exchange. On December 8, 2014, we alerted IRS management to our concerns regarding:

- The IRS's decision not to use Form 1095-A data as they become available, in conjunction with the EPD, to verify PTC claims at the time tax returns are processed. Original business requirements submitted to the Office of Information Technology requested that computer programming be developed to use the EPD to verify PTC claims until Form 1095-A data became available. However, in September 2014, IRS management decided to not complete the programming to use Form 1095-A data as they become available to verify PTC claims at filing and instead to rely solely on the EPD to verify PTC claims at filing.
- The IRS allowing PTC claims when it is unable to confirm insurance was purchased at an Exchange.

We recommended that the IRS:

- Revise computer programming business requirements to use Forms 1095-A as the primary third-party data to verify PTC claims at filing with the EPD used as a secondary source. For example, when a tax return is filed with a PTC claim, computer programs should match information from the tax return to the Form 1095-A data file to confirm the purchase of insurance through an Exchange. If this match does not confirm the individual purchased insurance from an Exchange, perform a secondary match to the EPD.
- Revise processes and procedures to freeze the portion of the refund attributed to the PTC when matches to both Forms 1095-A and the EPD do not confirm the individual purchased insurance through an Exchange. This process is similar to other prerefund examination and error resolution processes that the IRS uses whereby it suspends the processing of all or part of the tax return and requests additional documentation from the taxpayer. At a minimum, these processes should ensure that the taxpayer purchased insurance from an Exchange before the PTC claim is paid.

In response, IRS management indicated that the Form 1095-A is compiled using EPD. As such, the IRS believes that using the EPD will provide the same information as taxpayers are provided on Form 1095-A that they are required to receive from an Exchange. The IRS also responded that the Form 1095-A data will be available for review once received, and the IRS will use them to review specific individual situations. For example, Forms 1095-A data will be used by compliance operations to evaluate taxpayer data sent in as a result of a compliance activity.

In addition, IRS management indicated that they will use the IRS's existing capabilities to freeze refunds to prevent erroneous refunds if the information from the EPD does not match the information on the tax return and the IRS is unable to resolve the discrepancies. While these processes should enable the IRS to verify a significant number of PTC claims to Exchange data, it should be noted that the IRS could not verify Exchange enrollment for all individuals claiming the PTC at the start of the 2015 Filing Season because of the delays in receiving these data.

We are concerned with IRS management's decision to not revise computer programming to use Form 1095-A data when verifying PTC claims. As of March 5, 2015, the IRS indicated that four of the six states for which the IRS had no EPD as of January 20, 2015, had subsequently submitted EPD and Form 1095-A data. IRS management indicated that the IRS has not been able to load the EPD submitted in January and February into its processing systems for use in verifying PTC claims. As such, the IRS still does not have Exchange enrollment data for individuals living in these four states for use in verifying PTC claims before the claims are paid. Unlike the EPD, IRS management indicated that Form 1095-A data have been made available to IRS employees for use in researching discrepancies on PTC claims. Had the IRS completed the computer programming to verify PTC claims using EPD and Form 1095-A data as planned, the IRS would be able to ensure that all individuals claiming the PTC met the primary PTC eligibility requirement to obtain a QHP through an Exchange before the claim is paid.

Recommendation

Recommendation 1: The Director, Affordable Care Act Office, should revise computer programming business requirements to use Forms 1095-A data, in conjunction with the EPD, to verify PTC claimants enrolled in a QHP from an Exchange before tax refunds are paid.

> ***Management's Response:*** The IRS disagreed with this recommendation. The EPD contains the same plus additional information that is not reported on Forms 1095-A, and the EPD are available earlier than the Form 1095-A data, which allows the data to be available in the return processing systems at the start of the filing season. During the processing of tax returns, the IRS uses Form 1095-A data as a secondary source in conjunction with the EPD. In addition, to mitigate any delay in receipt of the EPD, the IRS developed and implemented a strategy that included contingency plans to ensure the accuracy of PTC claims and to prevent erroneous refunds from being paid. IRS contingency plans include contacting the taxpayer to obtain additional information when the IRS cannot determine whether the taxpayer enrolled in a QHP at the Exchange.

Office of Audit Comment: IRS management indicated that the EPD are available sooner than the Form 1095-A data. This is not an accurate statement. As our report details, the Federal Exchange did not provide the EPD for 1.7 million individuals, and six State Exchanges did not provide the EPD prior to the start of the 2015 Filing Season. IRS management informed us that the remaining data from the Federal Exchange and four of the six State Exchanges were not available for use in verifying tax returns until March 29, 2015, whereas the Forms 1095-A data were available to verify tax returns on February 18, 2015. In addition, while the IRS does use Form 1095-A data as a secondary source to verify PTC claims, the process is a manual process. Programming its computer system to match tax returns to Form 1095-A data when the EPD are missing or are not consistent with the tax return would improve the efficiency of the IRS's verification process and ensure that it is using its limited resources most effectively.

Guidance Does Not Fully Address Repayment of Advance Premium Tax Credits Paid During an Inconsistency Period

Our review of the Internal Revenue Code and the Department of Health and Human Services (HHS) regulations[8] found that the guidance does not fully address repayment of the APTC received during the months in which an enrollment inconsistency is being resolved if the individual is ultimately determined to not qualify for insurance through the Exchange. Such individuals are not entitled to the PTC. *********************2*********** *************************************2************************************* *************************************2************************************* *******2***********.

During the enrollment process, the Exchanges are responsible for verifying eligibility requirements to obtain a QHP through the Exchange and receive the APTC. The ACA allows individuals 90 days to provide supporting information to the Exchange when the Exchange is unable to verify that the individual met enrollment and/or APTC requirements. Individuals whose attested information qualifies them to receive the APTC are considered conditionally eligible and can receive APTC payments during this 90-day inconsistency period. At the end of the 90-day inconsistency period, the Exchange is to make a final determination as to an individual's eligibility to use the Exchange to purchase a QHP and/or receive the APTC. **2*** *************************************2************************************* ***********************************2*************************************** ***2*********. As a result, these individuals continue to receive APTC payments until such time as the Exchange finds the individuals to be ineligible.

On December 8, 2014, we recommended that the IRS seek guidance from the IRS Office of Chief Counsel to determine whether an individual is or is not entitled to all or a portion of

[8] 45 C.F.R. §§155. 300 – 355.

APTC payments received during an inconsistency period when the Exchange determines that the individual is ineligible or the inconsistency was not addressed. On December 8, 2014, IRS management indicated that they would forward our concern to the IRS Office of Chief Counsel. IRS management received guidance from its Health Care Counsel which states that persons who are not lawfully present in the United States are not eligible to receive the PTC and that all APTC must be repaid. However, this guidance does not address the need for repayment of the APTC received during inconsistency periods resulting from discrepancies in other eligibility requirements.

Recommendation

Recommendation 2: The Director, Affordable Care Act Office, should work with the Exchanges to **********************2***********************when an individual is determined to be ineligible subsequent to enrollment.

> ***Management's Response:*** The IRS partially agreed with this recommendation. The IRS provided instructions to the Exchanges for reporting EPD and Form 1095-A data when an individual who received the APTC is subsequently determined not to qualify for insurance through the Exchange and is therefore not entitled to the PTC. The IRS will review and update, as appropriate, current instructions for the recipients of Form 1095-A, instructions for Form 8962, Publication 974, *Premium Tax Credit (PTC)*, and IRS.gov to clarify the reconciliation requirements.
>
> ***Office of Audit Comment:*** The instructions do not include a requirement for the Exchanges **********************2******************** who received APTC payments during an inconsistency period and the Exchange determines the individual is ineligible. ************************2*********************************** *******************************2**********.

Employer and Insurer Reporting Relief Increases the Risk Ineligible Individuals Will Erroneously Receive Premium Tax Credits

The ACA requires the Exchanges to determine if applicants were offered health coverage by their employer. However, based on discussions with the Federal and State Exchanges, we determined that the majority of the Exchanges cannot verify most individuals' attestation that they were not offered health coverage by their employer, with the exception of those individuals who are eligible for a Government plan (such as Medicare, Medicaid, or Veterans Benefits).

Individuals are not eligible to receive the PTC if they are eligible for the MEC from an employer or government plan. Individuals are asked if their employer offered them health coverage when they apply to the Exchange to receive the APTC. The Exchanges are required to provide the applicants' response to this question along with information related to their employer to the IRS in the monthly EPD. Figure 3 shows how the Exchange application portrays this information.

Figure 3: Application for Health Coverage and Help Paying Costs

2. **Is anyone listed on this application offered health coverage from a job?**
Check yes even if the coverage is from someone else's job, such as a parent or spouse.
☐ **YES. If yes,** you'll need to complete and include Appendix A. Is this a state employee benefit plan? ☐ Yes ☐ No
NO. If no, continue to Step 5.

Source: Marketplace.cms.gov.

The ACA requires employers and insurers to file paper-filed Forms 1095-B and 1095-C for insurance offered during Calendar Year 2014 with the IRS no later than February 28, 2015, and electronically filed forms no later than March 31, 2015. These forms will provide the IRS with information to identify individuals to whom employers offered health insurance and whether the insurance offered was the MEC. The IRS can use the information provided on Forms 1095-B and 1095-C to verify that individuals claiming the PTC were not eligible for coverage from an employer. However, the receipt of required insurer (Form 1095-B) and employer (Form 1095-C) information reports has been delayed.

- **Form 1095-B** is filed by the insurer to report individuals who are covered by the MEC and was originally due to individuals on or before January 31, 2015, and due to the IRS by February 28, 2015. However, on July 9, 2013, the Department of the Treasury granted insurers transition relief from the Form 1095-B filing requirement. The transition relief was intended to give insurers time to adapt their health coverage and reporting systems to comply with the ACA. Under the transition relief, the filing deadline for paper-filed Forms 1095-B was delayed from February 28, 2015, to February 29, 2016, with electronically filed Forms 1095-B delayed from March 31, 2015, to March 31, 2016.

- **Form 1095-C** is filed by employers with 50 or more employees to provide information about offers of health coverage and enrollment in health coverage for their employees. The Form 1095-C was originally due to individuals on or before January 31, 2015, and due to the IRS by February 28, 2015. The same transition relief granted to insurers was also granted to employers. Under the transition relief, the filing deadline for paper-filed Forms 1095-C was delayed from February 28, 2015, to February 29, 2016, with electronically filed Forms 1095-C delayed from March 31, 2015, to March 31, 2016.

***********************************2*************************************
********2**********. As we noted previously, the information provided by the Exchanges regarding an individual's eligibility for employer-sponsored coverage may not be reliable due to the Exchanges inability to verify information provided during enrollment. IRS management indicated that the IRS will match PTC claims to information provided on Forms 1095-B and 1095-C beginning with Tax Year 2015. However, because these forms will generally not be

available until March 2016, which is after most taxpayers file their annual tax return, the match to Form 1095-B and Form 1095-C data will occur after tax return processing is completed.

Tools Were Developed to Assist the Internal Revenue Service and Taxpayers in Determining the Second Lowest Cost Silver Plan Premium

In order to accurately compute the PTC, the IRS and taxpayers must know the second lowest cost silver plan (SLCSP) premium cost applicable to their family size for each month of the year they receive coverage. The SLCSP refers to the level of coverage provided by a health plan. Health plans offered by the Exchange are categorized as Platinum, Gold, Silver, Bronze, or Catastrophic, depending on the share of costs the insurer covers.[9] The applicable SLCSP premium can change throughout the year. For example, changes in an individual's family size could affect the amount of the APTC an individual is entitled to receive in a given month. In addition, the SLCSP premium is based on the geographic location of where an individual resides. If the individual moves from one pricing location to another, the SLCSP will change and in turn affect the monthly APTC.

Exchanges should be notifying individuals at the time they enroll that they need to notify the Exchange if their circumstances change (*i.e.*, birth of a child or a change in income) throughout the year. This notification enables the Exchange to reassess an individual's eligibility to use the Exchange and adjust the amount of the APTC received, if necessary. The Exchanges are required to report the SLCSP premium to individuals and the IRS on Form 1095-A. However, if an individual does not report a change in circumstance, the amount of the SLCSP premium provided in monthly EPD data and on the Form 1095-A may not be accurate.

Form 8962 instructions caution individuals that the SLCSP premium reported on Form 1095-A may not be correct if they neglected to notify the Exchange of a change in their circumstances. Form 8962 instructions tell taxpayers to review Publication 974 for information on determining the correct premium for the applicable SLCSP. It should be noted that, as of January 26, 2015, the draft Publication 974 was not finalized and did not yet contain information that taxpayers would need to determine the correct SLCSP premium amounts.

On December 8, 2014, we notified the IRS of our concern regarding *********2***** ******2**********the SLCSP premium used by the taxpayer to calculate PTC claims on the Form 8962. We also raised a concern with the burden taxpayers may experience in obtaining the correct SLCSP premium to file their PTC claim and reconcile their APTC payments. We suggested the IRS work with the Exchanges to develop a tool that taxpayers can use to determine the benchmark SLCSP premium amount needed to accurately compute the PTC for their income

[9] A Silver plan will provide benefits that are actuarially equivalent to 70 percent of the full actuarial value of the benefits provided under the plan. This means the plan will cover about 70 percent of the costs for covered medical services.

and family size. The IRS can also use the data made available to taxpayers by the Exchanges to verify the SLCSP premium amounts provided by taxpayers on Form 8962.

IRS management responded that the Exchanges have an option of creating a self-help tool so taxpayers can look up their SLCSP or report the applicable SLCSP by month to all enrollees on Form 1095-A. The IRS has included links on IRS.gov to the individual State Exchanges and Healthcare.gov tools that can assist taxpayers in obtaining this amount. While these tools are intended to assist individuals who were not provided their SLCSP premium amount or who did not report a change in circumstance to the Exchange, individuals can also use these tools to verify the accuracy of the SLCSP premium provided on Form 1095-A.

In our ongoing review assessing the IRS's efforts to accurately verify PTC claims during the 2015 Filing Season, we plan to further assess the IRS's ability to verify the SLCSP premium in those instances in which a taxpayer reports an SLCSP premium amount on Form 8962 that does not match EPD data or information contained on Form 1095-A.

Additional Compliance Tools Are Needed to Prevent the Payment of Erroneous Premium Tax Credit Claims

The ACA included a number of provisions that once adhered to and implemented will provide the IRS with the information it needs to effectively identify erroneous PTC claims at the time tax returns are processed. However, even though the IRS will have the data it needs to identify erroneous claims moving forward, it does not have the tools it needs to effectively prevent PTC claims from being paid. The IRS can use existing math error authority[10] and electronic filing reject processes to adjust PTC claims when individuals do not provide certain required information (*e.g.*, the individual fails to attach Form 8962 when the APTC was received) or when a mathematical error on the tax return affects the accuracy of the claim.

However, the ACA did not grant the IRS the authority to systemically adjust a PTC claim when the claim is not supported by Exchange data (*e.g.*, the Exchange data show the individual did not use the Exchange to purchase insurance). As such, the IRS must audit PTC claims that are not supported by Exchange data before it can adjust the claim. The number of PTC claims the IRS can examine is limited to available resources. The IRS Examination function plan contains 36,000 PTC audits. In addition, the IRS plans to review approximately 75,000 PTC tax returns in the Automated Questionable Credits program for Fiscal Year 2015. IRS management indicated these numbers will continually be evaluated as returns are selected for treatment and may be increased or decreased as needed.

The IRS included a legislative initiative in its budget requests for Fiscal Years 2013, 2014, and 2015 to obtain authority to disallow tax benefit claims when reliable third-party data indicate the

[10] Math error authority allows the IRS to systemically disallow certain taxpayer claims at the time a tax return is processed.

claim is erroneous. This authority would enable the IRS to more effectively and efficiently identify and prevent the issuance of erroneous PTC claims before tax refunds are issued by allowing the IRS to systemically deny all PTC claims for which Exchange data show the claim is erroneous.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to assess the status of the IRS's preparations for verifying the accuracy of PTC claims during the 2015 Filing Season. To accomplish our objective, we:

I. Obtained an understanding of the role of the Federal and State Exchanges[1] and the processes and procedures in place to ensure that individuals are eligible to use the Exchange and receive the APTC.

   A. Obtained information from the HHS Office of Inspector General as to the role of the Federal and State Exchanges in the application processing and how the CMS will verify enrollment and eligibility.

   B. Visited the Federal Exchange and seven State Exchanges to obtain an understanding of how the Exchanges verify enrollment and eligibility for both electronic and paper applications and the status of the Exchanges' readiness to submit monthly EPD and annual reports (Form 1095-A, *Health Insurance Marketplace Statement*) to the IRS.

   C. Surveyed the remaining eight State Exchanges to obtain an understanding of how the Exchanges verify enrollment and eligibility for both electronic and paper applications and the status of the Exchanges' readiness to submit monthly EPD and annual reports (Forms 1095-A) to the IRS.

II. Assessed the adequacy of the IRS's plans to obtain, validate, and use third-party data (EPD and Forms 1095-A) provided to the IRS.

   A. Determined whether the IRS's processes ensure that all required data are included in the EPD and Forms 1095-A.

   B. Determined whether the Exchanges will fulfill the monthly reporting requirements by submitting the EPD.

   C. Determined whether the Exchanges are prepared to fulfill the annual reporting requirements by submitting Forms 1095-A to the IRS, identified the impact on individuals if the Exchanges are not ready to provide the Forms 1095-A, and identified any additional information taxpayers can use to claim the PTC if they do not receive a Form 1095-A.

[1] For the purposes of this report, the District of Columbia is included in "States" and "State Exchanges."

D. Determined whether the IRS adequately tested the EPD transmissions prior to the "go live" date.

E. Identified any additional third-party data that will be available to the IRS to verify PTC claims at filing.

III. Determined whether the IRS has adequate plans to validate the accuracy of APTC reconciliations and PTC claims at filing.

A. Determined whether the IRS is able to accept and accurately process returns containing PTC reporting requirements.

B. Determined how the IRS will confirm PTC eligibility requirements.

C. Obtained IRS estimates of how many taxpayers will claim the PTC during the 2015 Filing Season and staffing needs to verify tax returns with related PTC claims.

D. Determined how the IRS plans to identify and address potentially fraudulent requests for the PTC at filing.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: the policies and procedures the Federal and State Exchanges have in place for determining if a taxpayer is eligible to use the Exchange and receive the APTC and for submitting the EPD to the IRS for processing PTC claims at filing; the IRS's policies and procedures for developing tax forms, instructions, and publications to assist taxpayers with APTC reconciliation and PTC claims; the IRS's policies and procedures for obtaining, validating, and using the EPD provided by the Exchanges; and the IRS's policies and procedures for monitoring and validating the accuracy of APTC reconciliations and PTC claims at filing. We evaluated these controls by interviewing employees of Federal and State Exchanges, obtaining and reviewing the results of synthetic data testing prior to the "go live" date, interviewing IRS management, and reviewing key system documentation related to the verification and processing of APTC reconciliations and PTC claims at filing.

Appendix II

Major Contributors to This Report

Russell P. Martin, Acting Assistant Inspector General for Audit (Returns Processing and Account Services)
Deann L. Baiza, Director
Sharla J. Robinson, Audit Manager
Linna K. Hung, Lead Auditor
Laura P. Haws, Senior Auditor
Lance J. Welling, Senior Auditor
Jeffrey D. Cullum, Auditor
Nikole L. Smith, Auditor

Appendix III

Report Distribution List

Commissioner C
Office of Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Operations Support OS
Deputy Commissioner for Services and Enforcement SE
Chief Technology Officer OS:CTO
Commissioner, Wage and Investment Division SE:W
Director, Filing and Premium Tax Credit Strategy SE:ACA
Director, Program Management Office SE:ACA
Associate Chief Information Officer, Affordable Care Act (PMO) OS:CTO:ACA
Director, Submission Processing, Wage and Investment Division SE:W:CAS:SP
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Director, Affordable Care Act Office SE:ACA:ONE

Appendix IV

Health Care Exchanges

Thirty-six States used the Federal Exchange for eligibility and enrollment determinations during the 2014 Exchange health insurance enrollment period. Fifteen States, including the District of Columbia, operated their own Exchange. The number of States that make up the Federal Exchange and that operate their own State Exchange has changed for the 2015 enrollment period.

Federally Facilitated Exchange[1]			State-Based Exchanges
Alabama	Louisiana	Ohio	California
Alaska	Maine	Oklahoma	Colorado
Arizona	Michigan	Pennsylvania	Connecticut
Arkansas	Mississippi	South Carolina	District of Columbia
Delaware	Missouri	South Dakota	Hawaii
Florida	Montana	Tennessee	Kentucky
Georgia	Nebraska	Texas	Maryland
Idaho	New Hampshire	Utah	Massachusetts
Illinois	New Jersey	Virginia	Minnesota
Indiana	New Mexico	West Virginia	Nevada
Iowa	North Carolina	Wisconsin	New York
Kansas	North Dakota	Wyoming	Oregon
			Rhode Island
			Vermont
			Washington

Source: The CMS as of September 30, 2014.

[1] Idaho and New Mexico are in Supported State-Based Exchanges and the eligibility and enrollment process was completed by the Federally Facilitated Exchange.

Appendix V

Overview of Exchange Periodic Data Testing Phases

Each Exchange must complete a four-phase testing process with the IRS and the CMS before it can submit the EPD through the HHS Data Services Hub[1] to the IRS. An Exchange cannot advance to the next phase of testing until the results of the previous test phase are reviewed and validated. This testing helps ensure that the Exchanges' EPD are consistent with established data formats. The following table contains an overview of the testing phases the Exchanges must complete before transmitting monthly EPD to the IRS.

Testing Phase	Description
Phase I	State Readiness Phase – State Exchanges[2] test connectivity with the CMS.
Phase II	CMS Phase – Exchanges submit test transmissions to the HHS Data Services Hub and will receive mock responses from the Hub to ensure that the data submissions meet the required file formats and data are accurately maintained during transmissions.
	Testing Readiness Review – This review must be completed before beginning IRS testing in Phase III to ensure that the Exchange is ready to enter testing.
Phase III	IRS Phase – Test transmissions of various monthly report file data sets.
	Stage 1: Transmission of a single Monthly Report file generated by an Exchange with a successful response from the IRS for a single family for a single month to verify the Exchange can successfully send and receive a Monthly Report.
	Stage 2: Transmission of a Monthly Report for two coverage months to establish a baseline set of families for testing.
	Stage 3: Transmission of a Monthly Report for three coverage months including some changes in family circumstances for baseline families.
	Stage 4: Transmission of a Monthly Report for 11 coverage months with more complex changes in family circumstances for the household throughout the year.
Phase IV	Production Phase – Begin reporting monthly data.

Source: CMS and IRS interagency testing documents.

[1] The HHS maintains the Data Services Hub. The Exchanges will electronically transmit the EPD and Form 1095-A data through the Hub. No quality checks of the EPD or Form 1095-A data will be performed by the Hub.
[2] For the purposes of this report, the District of Columbia is included in "State Exchanges."

Appendix VI

Management's Response to the Draft Report

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

April 16, 2015

MEMORANDUM FOR RUSSELL P. MARTIN
ACTING, ASSISTANT INSPECTOR GENERAL FOR AUDIT

FROM: Carolyn A. Tavenner
Director, Affordable Care Act

SUBJECT: Draft Audit Report – Assessment of Internal Revenue Service Preparation for Processing Premium Tax Credit Claims (Audit 201440325)

Thank you for the opportunity to respond to the above-referenced report. We appreciate your acknowledgement of the Internal Revenue Service (IRS) efforts in administering the Premium Tax Credit (PTC) provision under Section 36B of the Internal Revenue Code. The IRS takes very seriously its role to ensure the accuracy and timely administration of the Affordable Care Act (ACA) provisions.

Section 36B was enacted as part of the Patient Protection and Affordable Care Act (PPACA) in March 2010. Beginning in 2014, the PTC helps to make health insurance more affordable for moderate-income families by providing assistance in paying for health insurance premiums. Individuals who obtain their health insurance through the Health Insurance Exchange and meet certain income requirements may be entitled to receive the PTC. Eligible individuals can elect to receive the PTC in advance as monthly payments directly to their insurance company as payment for their premium (the Advance PTC (APTC)), or wait and claim the PTC on their annual tax return. The IRS is responsible for determining the amount of PTC an individual is entitled to receive. The amount of PTC an individual is entitled to is based upon the actual income and family size reported on the annual tax return which can be different from the estimates used by the Exchange to determine allowable APTC. All individuals who elect to receive APTC must file a tax return to reconcile the advance payments.

Your review of this provision highlighted actions the IRS took to ensure accurate processing of PTC claims for tax year 2014 and acknowledged that we had contingency plans in place if Exchange Periodic Data (EPD) was not available, and we could not determine if a taxpayer had enrolled in a qualified health plan at the Exchange. The IRS not only has existing data tools and systems to address tax compliance generally, but the data from the Exchange also allows IRS to determine the taxpayer's qualification for the PTC. Prior to the start of the filing season, the IRS developed and implemented contingency plans to ensure all returns were passed through new and existing filters to detect and prevent erroneous refunds from being issued. IRS also took steps to prevent erroneous refunds when there was no evidence that a taxpayer went to the Exchange.

We are using a combination of fraud and other filters applied "at-filing" and post-processing compliance activities to address those claims that cannot be verified during the processing of the returns. In addition, the IRS is using its existing capabilities to withhold refunds and prevent erroneous refunds when the information from the EPD and Form 1095-*A Health Insurance Marketplace Statement,* does not match the information on the tax return. This gives the IRS time to correspond with the taxpayer for additional information to substantiate appropriate payments.

In addition, we appreciate your noting IRS efforts to provide taxpayers with self-assistance tools to determine their applicable Second Lowest Cost Silver Plan (SLCSP) premium amount. For example, IRS has provided links on irs.gov to the individual State Marketplaces and Healthcare.gov tools. Per CMS, these tools are intended to assist individuals who were not provided their SLCSP premium amount on Form 1095-A; or who had a change in circumstances not reported to the Exchange during the coverage year.

Attached are our comments to your recommendations. If you have any questions, please contact me, or Johnny Witt, Deputy Director, Affordable Care Act Office, 202-317-3764.

Attachment

RECOMMENDATION 1:
The Director, Affordable Care Act Office, should revise computer programming business requirements to use Forms 1095-A in conjunction with the EPD to verify PTC claimants enrolled in a QHP from an Exchange before tax refunds are paid.

CORRECTIVE ACTION:
The IRS disagrees with this recommendation. The EPD contains the same plus additional information that is not reported on the Form 1095-A, and EPD is available earlier than the Form 1095-A which allows the data to be available in our return processing systems at the start of the filing season. During the processing of tax returns, the IRS uses the Form 1095-A as a secondary source in conjunction with the EPD. In addition, to mitigate any delay in receipt of EPD, the IRS developed and implemented a strategy which included contingency plans to ensure the accuracy of PTC claims and to prevent erroneous refunds from being paid. Our contingency plans include contacting the taxpayer to obtain additional information when we cannot determine whether the taxpayer enrolled in a qualified health plan at the Exchange.

IMPLEMENTATION DATE:
N/A

RESPONSIBLE OFFICIAL(S):
N/A

RECOMMENDATION 2:
The Director, Affordable Care Act Office, should work with the Exchanges to *******2******** ******2******* when an individual subsequent to enrollment is determined to be ineligible.

CORRECTIVE ACTION:

The IRS partially agrees with this recommendation. We provided instructions to the Exchanges for reporting EPD and Form 1095-A when an individual who received APTC is subsequently determined not to qualify for insurance through the exchange and is therefore, not entitled to the PTC. The IRS will review and update, as appropriate, current instructions for Recipient on Form 1095-A, Instructions for Form 8962, Publication 974, and irs.gov to clarify the reconciliation requirements.

IMPLEMENTATION DATE:
12/31/2015

RESPONSIBLE OFFICIAL(S):
Director, SE Affordable Care Act Office