



## Treasury Inspector General for Tax Administration Office of Audit

### THE AFFORDABLE CARE ACT: AN IMPROVED STRATEGY IS NEEDED TO ENSURE ACCURATE REPORTING AND PAYMENT OF THE MEDICAL DEVICE EXCISE TAX

Issued on July 17, 2014

## Highlights

Highlights of Report Number: 2014-43-043 to the Internal Revenue Service Commissioners for the Small Business/Self-Employed Division and the Wage and Investment Division.

### IMPACT ON TAXPAYERS

The Affordable Care Act includes a tax provision that provides for an excise tax equal to 2.3 percent of the sales price for medical devices sold beginning January 1, 2013. Manufacturers, producers, and importers are responsible for collecting the medical device excise tax and must file a Form 720, *Quarterly Federal Excise Tax Return*. The Joint Committee on Taxation estimated revenues from the medical device excise tax of \$20 billion for Fiscal Years 2013 through 2019.

### WHY TIGTA DID THE AUDIT

This audit was initiated as part of our continued coverage of the IRS's implementation of key Affordable Care Act tax provisions. The overall objective of this review was to assess the IRS processing of tax returns reporting the medical device excise tax and efforts to identify taxpayer noncompliance.

### WHAT TIGTA FOUND

Our review found that both the number of Forms 720 filed reporting the medical device excise tax and the amount of associated revenue reported are lower than estimated. The IRS is attempting to develop a compliance strategy to ensure that businesses are compliant with medical device excise tax filing and payment requirements and has taken several measures to advise medical device manufacturers of the new excise tax. However, the IRS cannot identify the population of medical device manufacturers registered with the Food and Drug Administration that are required to file a Form 720 and pay the excise tax.

In addition, processing controls do not ensure the accuracy of medical device excise tax figures reported on paper-filed Forms 720. Our analysis of

5,107 Forms 720 processed for the quarters ending March 31 and June 30, 2013, identified discrepancies in the amount of the medical device excise tax and/or taxable sales amount captured from 276 paper-filed tax returns. TIGTA identified medical device excise tax discrepancies totaling almost \$117.8 million when comparing the excise tax amount captured by the IRS from the Form 720 to the excise tax amount TIGTA calculated.

Finally, the IRS erroneously assessed 219 failure to deposit penalties totaling \$706,753 against businesses filing a Form 720 for the quarters ending March 31, 2013, and June 30, 2013, which was designated a penalty relief period. The IRS had reversed 133 of the 219 penalty assessments. When TIGTA alerted the IRS of the remaining 86 penalties, IRS management reversed the penalties and issued apology letters to the affected taxpayers.

### WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS continue refining its compliance strategy to include actions that can be taken to identify noncompliant manufacturers. TIGTA also recommended that the IRS conduct a review of the 276 tax returns TIGTA identified to determine the proper excise tax owed, establish a process to verify the accuracy of the medical device excise tax amount for paper-filed Forms 720, and initiate a process to correspond with taxpayers to obtain missing taxable sales or tax amounts.

The IRS agreed with our recommendations and plans to consider alternative strategies for identifying noncompliant manufacturers, identify programming changes needed to improve the math verification for paper-filed Forms 720, and implement procedures for corresponding with taxpayers if the changes can be accomplished within budgetary constraints. The IRS also indicated that approximately two-thirds of the paper-filed tax returns TIGTA identified were reviewed.

### READ THE FULL REPORT

To view the report, including the scope, methodology, and full IRS response, go to:

<http://www.treas.gov/tigta/auditreports/2014reports/201443043fr.pdf>

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