



*Affordable Care Act: Controls Over Financial
Accounting for the Premium Tax Credit
Should Be Improved*

March 2, 2016

Reference Number: 2016-13-021

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.

Phone Number / 202-622-6500

E-mail Address / TIGTACommunications@tigta.treas.gov

Website / <http://www.treasury.gov/tigta>



To report fraud, waste, or abuse, call our toll-free hotline at:

1-800-366-4484

By Web:

www.treasury.gov/tigta/

Or Write:

Treasury Inspector General for Tax Administration
P.O. Box 589
Ben Franklin Station
Washington, D.C. 20044-0589

Information you provide is confidential and you may remain anonymous.



HIGHLIGHTS

AFFORDABLE CARE ACT: CONTROLS OVER FINANCIAL ACCOUNTING FOR THE PREMIUM TAX CREDIT SHOULD BE IMPROVED

Highlights

Final Report issued on March 2, 2016

Highlights of Reference Number: 2016-13-021 to the Internal Revenue Service Chief Financial Officer.

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 eligible individuals with the cost of their health insurance premiums. Rather than wait to claim the credit on their Federal tax returns, individuals may elect to have the PTC paid directly to their health insurance issuers as partial payment for their monthly premiums (referred to as the Advance Premium Tax Credit or APTC). In addition, as a refundable credit, the PTC is fully payable to the taxpayer even if the tax credit exceeds the tax liability.

WHY TIGTA DID THE AUDIT

This audit was initiated as the result of a congressional request for a review of the administration of the PTC. This review was performed as part of a series of coordinated audits and evaluations by the Department of Health and Human Services Office of Inspector General and TIGTA. The objective of this review was to evaluate IRS financial accounting controls for the PTC.

WHAT TIGTA FOUND

TIGTA identified that controls over the financial accounting for fund outlays (disbursements) associated with the PTC should be improved. Specifically, TIGTA found errors in the IRS financial accounting and reporting of PTC-related fund outlays. To reconcile the PTC, the IRS must adjust the amounts initially recorded for APTC payments based on taxpayer-estimated income and family size to

the actual PTC amount based on income and number of dependent deductions reported on the taxpayer's Federal tax return. The errors we identified were due to a programming miscalculation. The miscalculation was not caught due to insufficient testing of the financial system programming developed to account for the impact of the reconciliation of PTC fund outlays (disbursements).

Due to this programming error, the IRS understated the amount of PTC disbursements and overstated the balance in the IRS PTC account by \$447 million. Further, the error TIGTA identified in the financial accounting records, if left uncorrected, would have resulted in a misstatement of the Fiscal Year 2015 IRS financial statements refundable credits in excess of tax liability account.

In addition, TIGTA determined that the key controls established over PTC accounting do not include the requirement for the periodic performance of a financial reconciliation of the IRS's records and the APTC payment information (by taxpayer) prepared and reported by the Health Insurance Marketplaces.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Chief Financial Officer, in coordination with the Chief Technology Officer, develop procedures requiring the timely and comprehensive review and testing of any changes to the financial system programming used to report outlays related to the PTC. In addition, the Chief Financial Officer, in coordination with the Affordable Care Act Office, should work with the Centers for Medicare and Medicaid Services to jointly develop procedures for the periodic financial reconciliation of APTC information.

In their response, IRS management agreed with our recommendations. The IRS plans to ensure that established test standards and guidelines are adhered to during financial systems testing. In addition, the IRS plans to perform periodic reconciliations of APTC payment information provided by the Health Insurance Marketplaces to its financial records.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 2, 2016

MEMORANDUM FOR CHIEF FINANCIAL OFFICER

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved (Audit # 201510312)

This report presents the result of our review to evaluate the Internal Revenue Service (IRS) financial accounting controls for the Premium Tax Credit (PTC). This review was initiated as the result of a congressional request to review the administration of the PTC. This review is included in our Fiscal Year 2016 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 V.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. If you have any questions, please contact me or Gregory D. Kutz, Assistant Inspector General for Audit (Management Services and Exempt Organizations).



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

Table of Contents

Background.....Page 1

Results of ReviewPage 5

 The Internal Revenue Service Did Not Accurately Track and Report
 Premium Tax Credit OutlaysPage 5

Recommendation 1:.....Page 6

 Additional Steps Are Needed to Ensure That Advance Premium Tax
 Credit Payment Financial Accounting Information Is Accurate.....Page 7

Recommendation 2:.....Page 8

Appendices

 Appendix I – Detailed Objective, Scope, and MethodologyPage 9

 Appendix II – Major Contributors to This ReportPage 12

 Appendix III – Report Distribution ListPage 13

 Appendix IV – Outcome MeasurePage 14

 Appendix V – Management’s Response to the Draft ReportPage 15



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

Abbreviations

ACA	Patient Protection and Affordable Care Act
APTC	Advance Premium Tax Credit
CFO	Chief Financial Officer
CMS	Centers for Medicare and Medicaid Services
EPD	Exchange Periodic Data
FY	Fiscal Year
IITC	Individual Income Tax Credits
IRS	Internal Revenue Service
OMB	Office of Management and Budget
PTC	Premium Tax Credit
RRACS	Redesigned Revenue and Accounting Control System
TIGTA	Treasury Inspector General for Tax Administration



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

Background

Refundable tax credit created by the Affordable Care Act

The Patient Protection and Affordable Care Act (hereafter referred to as the ACA)¹ created a new refundable² tax credit, the Premium Tax Credit (PTC), to assist eligible taxpayers with paying their health insurance premiums. Funding for the PTC is provided by a permanent indefinite appropriation to the Department of the Treasury.³ The ACA also created the Health Insurance Marketplace (hereafter referred to as the Marketplace). The Marketplaces are where individuals (and their families) find information about health insurance options, purchase qualified health plans, and, if eligible, obtain help in paying premiums. According to the U.S. Department of Health and Human Services, as of February 2015, qualified health plans selections and automatic reenrollments were 11.7 million.

When enrolling in a qualified health plan⁴ through the Marketplace, eligible individuals can choose to have some or all of the PTC paid in advance to their health insurance company as payment of their monthly premium (hereafter referred to as the Advance Premium Tax Credit or APTC). Alternatively, individuals can pay the premium and wait to claim all of the PTC on their Federal income tax return.

Implementation of the APTC payment

The Centers for Medicare and Medicaid Services (CMS)⁵ oversees implementation of certain ACA provisions related to the Marketplace. The CMS operates the Federally Facilitated Marketplace and works with the States to establish State partnership Marketplaces, including overseeing their operations. The Marketplaces have responsibility for determining if an individual is eligible to purchase health insurance through the Marketplace as well as determining the amount of the APTC they are eligible to receive. Total APTC disbursements⁶

¹ Pub. L. No. 111-148, 124 Stat. 119 (2010) (codified as amended in scattered sections of the Internal Revenue Code and 42 U.S.C.), 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 The Internal Revenue Service has implemented the PTC program on behalf of the Department of the Treasury.

⁴ A qualified health plan is an insurance plan that is certified by the Health Insurance Marketplace and provides essential health benefits, follows established limits on cost-sharing (like deductibles, copayments, and out-of-pocket maximum amounts), and meets other requirements.

⁵ The CMS has implemented the PTC program on behalf of the Department of Health and Human Services.

⁶ Disbursements are amounts paid by Federal agencies, by cash or cash equivalent, during the fiscal year to liquidate Government obligations.



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

for Fiscal Year (FY) 2014⁷ were nearly \$11 billion (\$15.5 billion in Calendar Year 2014). These disbursements went to 291 health insurance issuers. The IRS reported that as of September 30, 2015, total credits claimed on 2014 tax returns totaled \$9.8 billion.

Once a Marketplace determines the amount of the APTC an individual is eligible to receive, the individual then elects the amount to be sent to their health insurance issuer on a monthly basis. The CMS subsequently sends a request to the Department of the Treasury's Bureau of the Fiscal Service⁸ to issue monthly APTC payments to the individual's health insurance issuer. These payments are certified by the CMS and paid from an allocation account⁹ established for the use of the CMS.

Reconciliation of the PTCs

Ultimately, the Internal Revenue Service (IRS) is responsible for determining the amount of the PTC a taxpayer receives based on his or her tax return. All individuals who chose to have APTC payments sent to a health insurance issuer are required to file a Federal tax return to reconcile the APTC with the actual PTC they are eligible to receive.¹⁰ This reconciliation is necessary because a Marketplace's computation of the APTC is based on estimates of an individual's anticipated income and family size for the upcoming calendar year. The amount of the PTC that taxpayers are entitled to receive is based on their actual income and family size (number of exemptions) as reported on their annual Federal tax return, which may be different from the estimates used by the Marketplace to determine the allowable APTC.

The ACA requires Marketplaces to provide the IRS with information regarding individuals enrolled in a Marketplace Exchange on a monthly basis (referred to as Exchange Periodic Data or EPD). This information includes monthly (and year-to-date cumulative) amounts of the APTC paid to health insurers on behalf of taxpayers. During the Calendar Year 2014 health insurance enrollment period, the District of Columbia and 14 States operated their own Exchanges, while the remaining 36 States partnered with the Federal Exchange which constitutes the Marketplace. In addition, the Marketplaces provide an annual summary to both the IRS and

⁷ For FY 2014, APTC disbursements began in January 2014. A fiscal year is any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.

⁸ A new bureau of the Department of the Treasury formed from the consolidation of the Financial Management Service and the Bureau of the Public Debt. Its mission is to promote the financial integrity and operational efficiency of the U.S. Government through exceptional accounting, financing, collections, payments, and shared services.

⁹ Allocation accounts are authorized and appropriate when a law requires funds that are appropriated to one department to be transferred to pay for activities that are the statutory responsibility of a second department.

¹⁰ Taxpayers who enrolled in a qualified health plan through the Marketplace in Calendar Year 2014 will receive a Form 1095-A, *Health Insurance Marketplace Statement*, from the Marketplace. Information from this form should be used to calculate the amount of the taxpayer's PTC and reconcile the APTCs made on the taxpayer's behalf to the health insurance issuer. To do this, the taxpayer will use Form 8962, *Premium Tax Credit (PTC)*, when filing his or her tax return.



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

the enrolled individuals detailing specific information. This summary is referred to as Form 1095-A, *Health Insurance Marketplace Statement*.

Funding the PTC

After significant planning and review, the IRS, Department of the Treasury, Department of Health and Human Services, the CMS, and the Office of Management and Budget (OMB) agreed that creating an allocation account for the CMS to use in obligating and disbursing funds for the APTC was the most logical and efficient approach to administering the PTC. As part of this approach, the CMS is responsible for certifying the availability of funds (via the allocation account) for APTC payments to health insurance issuers.

The CMS is also responsible for leading the Federal Marketplace, managing relationships with State Marketplaces, and providing oversight for the agents and brokers who enroll qualified individuals in qualified health plans and assist them in applying for the APTC. Under this approach, APTC payments will be captured in the “child” (allocation) account, and all reconciliation (refund) outlays will be captured in the “parent” account of the refund appropriation. The IRS is responsible for the unified reporting of all PTC appropriation activity on its annual financial statements.

Tracking PTC outlays with IRS financial systems

The financial accounting for refundable tax credits is a complex multistep process. The PTC, as a refundable tax credit, is fully payable to the taxpayer even if the tax credit exceeds the tax liability, thereby providing greater economic benefit. The Department of the Treasury permanent Indefinite Refund Appropriation provides funding for the PTC. The Department of the Treasury account 20x0949 is used to track PTC funds within the IRS general ledger. Accurately tracking the total outlays (disbursements) associated with the PTC involves two steps.

First, the IRS records monthly the summary amount of the fund outlay (APTC payments made by the CMS to health insurers) in its general ledger based on PTC reports provided by the CMS. Second, the IRS records an adjustment to these outlays to reflect information on filed tax returns claiming the PTC. The overall objective of this two-part process is to allow the IRS to accurately record and report on the total amount of funding outlays associated with instances in which the total PTC exceeded the taxpayer’s liability.

Calculation of the PTC funds outlays adjustment

This calculation is performed within the Individual Income Tax Credits (IITC) Report programming using taxpayer data extracted from the IRS Master File.¹¹ The results of this

¹¹ The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

calculation are posted to the Redesigned Revenue and Accounting Control System (RRACS), which serves as the IRS's general ledger for custodial accounting.

This review was initiated as the result of a congressional request for a review of the administration of the PTC. This report addresses the IRS's controls over the financial accounting (hereafter referred to as accounting) of the PTCs. Our audit objective was limited to assessing the ability of the IRS to accurately calculate, record, and report the outlay (disbursement) amount associated with the PTC. We did not perform any detailed testing to evaluate the IRS's efforts to ensure the accuracy of the underlying source information in the taxpayer's record that the IITC Report programming used in calculating the FY 2015 PTC outlay (disbursement) amount. An evaluation of controls over the accuracy of this underlying support information is the subject of a separate Treasury Inspector General for Tax Administration (TIGTA) audit scheduled to be completed in FY 2016.

This review was performed at the IRS Headquarters office of the Chief Financial Officer (CFO) in Washington, D.C., during the period October 2014 through October 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.



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

Results of Review

The Internal Revenue Service Did Not Accurately Track and Report Premium Tax Credit Outlays

TIGTA identified that controls over the financial accounting for fund outlays (disbursements) associated with the PTC should be improved. Specifically, errors were identified in the IRS financial accounting and reporting of PTC-related fund outlays during our testing conducted in June 2015. To reconcile the PTC, the IRS must adjust the amounts initially recorded for APTC payments in the IRS financial records. These amounts were based on taxpayer-estimated income and family size. These amounts must be adjusted to reflect the actual PTC amount based on income and number of dependent deductions reported on the taxpayer's Federal tax return. The errors we identified were due to a programming miscalculation. This miscalculation was not caught because of insufficient testing of the financial system programming developed to account for the impact of this reconciliation of PTC fund outlays (disbursements).

Due to this programming error, the IRS understated the amount of PTC disbursements and overstated the balance in the IRS account used to track PTC funds in its financial records by \$447 million.¹² This resulted in an inaccuracy in the IRS quarterly report to the OMB on the amount of PTC funds outlays. Further, the error we identified in the financial accounting records, if left uncorrected, would have resulted in a misstatement of the IRS FY 2015 financial statements account refundable credits in excess of tax liability.

In order to accurately track and report fund outlays associated with refundable credits such as the PTC, the IRS must calculate the amount of the tax credit(s), in total, that exceeded the tax liability that an individual taxpayer is claiming for the credit(s) on his or her Federal tax return. In performing this calculation, the IRS uses the IITC Report programming. Although the IRS updated the financial system programming for the IITC Report programming in February 2015 to include the PTC, our review of a random sample of 50 tax returns claiming the PTC found that in 14 (28 percent) cases, the PTC outlay amount was not calculated accurately. The IRS informed us that in all 14 cases, the IITC Report programming did not properly consider the impact of other

¹² We did not perform detailed testing of the accuracy of information reported to the OMB; however, when we advised the IRS of the programming error they informed us that the second quarter reporting to the OMB was inaccurate and it will be corrected in the third quarter and the year-to-date figure in the third quarter will be accurate.



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

credits¹³ claimed by the taxpayer when calculating the PTC outlay amount. As a result, the calculation of the PTC adjustment was incorrect.

After the errors were identified, the IRS revised the programming it uses to calculate PTC funds outlays and adjusted its financial records. This adjustment increased the June 2015 year-to-date net PTC funds outlay amount by \$447 million (3 percent) as illustrated in Figure 1. The revised programming was completed in time for the IRS to provide corrected third quarter FY 2015 IITC reporting to the OMB. We determined that the revised outlay calculation programming correctly processed all of the 50 cases we sampled including the 14 error cases.

Figure 1: Summary of Correction to the IRS’s PTC Funds Outlay Records (Third Quarter FY 2015 Year to Date)

	Amounts Before Programming Correction (millions)	Amounts After Revised Programming (millions)	Difference (millions)
Total APTC Funds Outlay	\$17,260 ¹⁴	\$17,260	-
PTC Funds Outlay Adjustment	<u>(\$3,065)</u>	<u>(\$2,618)</u>	<u>\$447</u>
Net PTC Funds Outlay	\$14,195	\$14,642	\$447

Source: Information regarding amounts before programming correction was provided by the IRS CFO. Amounts after revised programming reflect information provided in the IRS IITC Report (third quarter FY 2015).

The accounting errors identified are primarily attributable to the lack of comprehensive testing by the CFO of the financial system programming for the IITC Report program update to track outlay transactions related to the PTC. Specifically, our review found that although the IRS CFO informed us that some limited testing of the programming was performed, this testing was insufficient to ensure that the results produced were correct for various accounting scenarios such as taxpayers claiming multiple credits. It is important to note that the accounting errors we identified affected only the way in which the IRS recorded PTC transactions in its records for financial reporting purposes and did not affect the actual processing of the tax return by the IRS.

Recommendation

Recommendation 1: The CFO, in coordination with the Chief Technology Officer, should develop procedures requiring the timely and comprehensive review and testing of any changes to the financial system programming used to report outlays related to the PTC.

¹³ Other refundable credits include for example, the Earned Income Tax Credit and the Child Tax Credit. In determining the excess credit over tax liability amount related to the PTC, the IRS must identify all refundable credits and then apply the total excess credit amount based on a pre-established formula.

¹⁴ This number did not require adjustment because it was not affected by the programming error.



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

Management's Response: The IRS agreed with this recommendation. The CFO and Chief Technology Officer will ensure that established test standards and guidelines are adhered to during financial systems testing, including testing of the IITC Report and validating APTC and PTC reconciliation reporting. The IRS Chief Technology Officer will ensure adherence to these standards and guidelines through increased monitoring and discussion during regular progress meetings and by employing more frequent written reminders. Any additional testing is contingent on additional resources or the reprioritization of current workload.

Additional Steps Are Needed to Ensure That Advance Premium Tax Credit Payment Financial Accounting Information Is Accurate

The key controls established by the IRS and the CMS over PTC accounting do not include the requirement for the periodic performance of a financial reconciliation of APTC total outlays per the IRS's records and the APTC payment information (by taxpayer) prepared and reported by the Marketplaces. A financial reconciliation of this information would provide enhanced assurance that the information received by the IRS from the Marketplaces is complete, and total funds outlays, as recorded in the IRS's accounting records, are supported in total by detailed information tracked and reported by the Marketplaces. This financial reconciliation is also critical because the IRS is responsible for reporting financial activity related to the APTC in its annual audited financial statements. In addition, this periodic reconciliation would support an evaluation of the annual summary information provided at year-end by the Marketplaces to taxpayers and the IRS. In Calendar Year 2014, the IRS recorded approximately \$15.5 billion in APTC disbursements to health insurers based on information provided by the CMS, which is the basis for the IRS's recording of APTC outlays in its general ledger.

The ACA requires the Marketplaces to provide the IRS with information regarding individuals who are enrolled in qualifying health plans by the Exchange on a monthly basis. This information is referred to as the EPD. The monthly and year-to-date cumulative EPD stipulate the amount of the APTC paid to health insurers on behalf of taxpayers, which should reconcile to the outlay information received by the IRS from the CMS after accounting for timing differences and any adjustments, such as in process corrections of prior payment errors.

The Marketplaces are also required to provide an annual summary to both the IRS and the individual detailing specific information related to the individual's enrollment. This is referred to as Form 1095-A. The Form 1095-A includes the amount of the APTCs paid for under the qualified health plan.

However, Marketplace information reported to the IRS, in the EPD as of May 2015, was incomplete and did not include APTC disbursement data from two exchanges on data that TIGTA received from the IRS. Marketplace information separately reported to the IRS in the Form 1095-A as of May 2015 was similarly incomplete and did not include APTC disbursement data from two exchanges based on data that TIGTA received from the IRS. While this



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

incomplete information adversely affected the IRS's ability to reconcile total Calendar Year 2014 APTC outlays, requiring a financial reconciliation would still provide strong benefits to the overall financial accounting process going forward.

First, the performance of a periodic reconciliation would provide a baseline for determining the magnitude of the difference between total APTC outlays and the APTCs reported by the Marketplaces. Second, because the Department of Health and Human Services Office of Inspector General has previously reported that the CMS cannot reconcile payments made to health insurers to APTC payments made to taxpayers,¹⁵ a financial reconciliation between total APTC outlays and APTC payments reported via the EPD would provide the IRS with significantly enhanced assurance regarding accuracy of the amount of APTC advances it reports in its financial records. Finally, we have communicated this accounting issue to the Department of Health and Human Services Office of Inspector General for follow-up.

Recommendation

Recommendation 2: The CFO, in coordination with the ACA Office, should work with the CMS to jointly develop procedures for the periodic financial reconciliation of APTC information.

Management's Response: The IRS agreed with this recommendation. On a quarterly basis, the IRS will reconcile the EPD to the CMS disbursements paid to the Marketplace insurance companies. These reconciliations will be prepared at a summary level and the IRS will work with the CMS to evaluate any significant variances.

¹⁵ In June 2015, the Department of Health and Human Services Office of Inspector General reported that the CMS is unable to verify the amounts requested through qualified health plan issuers' attestations on an enrollee-by-enrollee basis because it obtains APTC payment data from qualified health plan issuers on only an aggregate basis.



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to evaluate IRS financial accounting controls for the PTC. To accomplish this objective, we:

- I. Evaluated the effectiveness of the process and controls developed for the financial accounting of the PTC.
 - A. Obtained and reviewed any policies, procedures, and guidelines applicable to the financial accounting for Federal tax credits and allocation account activity.
 - B. Reviewed controls over posting of APTC outlay information to the IRS's records.
 1. Compared IRS postings to the RRACS to CMS monthly trial balance activity for Calendar Year 2014 and FY 2015 (through June 2015) and investigated any differences identified.
 2. Compared summary RRACS APTC-related information for Calendar Year 2014 and FY 2015 (through June 2015) to Bureau of the Fiscal Service account activity records and investigated any differences identified.
 - C. Assessed the results of the IRS's review of monthly input received from the CMS and evaluated any actions taken as a result of significant variances identified.
 - D. Determined the status of the IRS's efforts to update its IITC Report programming to include PTC information.
 - E. Reviewed the methodology used to update the IITC Report programming to account for PTC outlays and evaluated the accounting scenarios developed in support of this process.
 - F. Evaluated controls over the process for posting outlay adjustments to the RRACS for taxpayers claiming the PTC on tax returns.
 1. Evaluated the audit trail maintained for posting outlay adjustments to the RRACS and reviewed whether it contains sufficient detail to identify transaction-level (taxpayer) adjustment information.
 2. Identified the population of all tax returns filed from January 1 to April 2, 2015, claiming the PTC using information from data stored at TIGTA's Data Center Warehouse¹ (extracted from the Individual Return Transaction File). To assess

¹ TIGTA's Data Center Warehouse is used to maintain data that have been extracted from the IRS's data storage.



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

the reliability of this information, we ensured the extract contained the specific data elements requested and compared selected data in the extract with information in the Integrated Data Retrieval System for items we sampled in Step I.F.3.

3. Using the population of tax returns identified in Step I.F.2., selected a random sample of 50 tax returns and for each tax return identified the associated adjustment to PTC outlay information contained in the IITC Report programming audit trail. We selected our sample randomly from 1,570,920 taxpayers who filed IRS Form 8962, *Premium Tax Credit (PTC)*, from January 1 to April 2, 2015. Our testing was limited to evaluating the programming for the various accounting scenarios identified in Step I.E. and we selected a sample of 50 tax returns in order to ensure that all scenarios identified were tested. We did not perform the testing necessary to validate whether the population we identified included all taxpayers that filed IRS Form 8962. We used the Statistical Analysis System random number generator to select a random sample of 50 tax returns. Our sampling methodology was reviewed by our contracted statistician.
 4. Reviewed the adjustment amounts for the 50 sampled tax returns for consistency with the accounting scenarios analyzed in Step I.E. and investigated any differences.
 5. Reviewed posting of IITC Report programming results for the PTC to the Bureau of the Fiscal Service account activity records for the period January through June 2015.
 6. Reviewed any reconciliations performed between the Calendar Year 2014 APTC disbursements reported to the IRS by the CMS monthly and total Calendar Year 2014 APTC payments reported to the IRS by Health Insurance Marketplaces.
- II. Evaluated the steps taken to timely and accurately report PTC information to stakeholders.
- A. Reviewed any procedures developed regarding the reporting of PTC information on the IRS's FY 2015 annual financial statements.
 - B. Determined whether the IRS reports total PTC outlays to the OMB and other stakeholders.



Affordable Care Act: Controls Over Financial Accounting for the Premium Tax Credit Should Be Improved

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 IRS's policies and procedures for recording and validating financial information related to the PTC. We evaluated these controls by interviewing IRS management, reviewing documentation related to the recording of PTC financial information, and evaluating PTC financial information reconciliation procedures.



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

Appendix II

Major Contributors to This Report

Gregory D. Kutz, Assistant Inspector General for Audit (Management Services and Exempt Organizations)

Alicia P. Mrozowski, Director

Anthony Choma, Audit Manager

Kanika Kals, Lead Auditor

Brandon Crowder, Senior Auditor



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

Appendix III

Report Distribution List

Commissioner
Office of the Commissioner – Attn: Chief of Staff
Deputy Commissioner for Operations Support
Deputy Commissioner for Services and Enforcement
Chief Technology Officer
Director, Affordable Care Act Office
Director, Filing and Premium Tax Credit Strategy, Affordable Care Act Office
Director, Program Management Office, Affordable Care Act Office
Associate Chief Information Officer, Affordable Care Act (PMO)
Director, Office of Audit Coordination



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

Appendix IV

Outcome Measure

This appendix presents detailed information on the measurable impact that our recommended corrective action will have on tax administration. This benefit will be incorporated into our Semiannual Report to Congress.

Type and Value of Outcome Measure:

- Reliability of Information – Actual (correction reflected in third quarter FY 2015 reporting to the OMB on Refundable Credit Outlays); \$447 million (see page 5).

Methodology Used to Measure the Reported Benefit:

Our review found that the IRS understated the amount of PTC disbursements and overstated the balance in the IRS account used to track PTC funds in its financial records by \$447 million. The errors we identified were due to a programming miscalculation. This miscalculation was not caught because of insufficient testing of the financial system programming developed to account for the impact of this reconciliation of PTC fund outlays (disbursements). This resulted in an inaccurate IRS quarterly report to the OMB on the amount of PTC funds outlays. After the errors were identified, the IRS revised the programming it uses to calculate PTC funds outlays and adjusted its financial records. This adjustment increased the year-to-date net PTC funds outlay amount by \$447 million (3 percent). The revised programming was completed in time for the IRS to provide corrected third quarter FY 2015 IITC reporting to the OMB.



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

Appendix V

Management's Response to the Draft Report



CHIEF FINANCIAL OFFICER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

February 10, 2016

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Jeffrey S. Wallbaum
Acting Chief Financial Officer

SUBJECT: Draft Audit Report – Affordable Care Act: Controls Over
Financial Accounting for the Premium Tax Credit Should Be
Improved (Audit # 201510312)

Thank you for the opportunity to respond to your draft audit report, "Affordable Care Act: Controls over Financial Accounting for the Premium Tax Credit Should Be Improved." We agree with your recommendations and have developed corrective actions to address them, as listed in the attachment.

If you have any questions, please contact me or a member of your staff may contact Howard Marcus, Deputy Associate CFO for Financial Management, at (202) 803-9688.

Attachment



*Affordable Care Act: Controls Over Financial Accounting for the
Premium Tax Credit Should Be Improved*

ATTACHMENT

RECOMMENDATION 1

The CFO, in coordination with the Chief Technology Officer, should develop procedures requiring the timely and comprehensive review and testing of any changes to the financial system programming used to report outlays related to the PTC.

CORRECTIVE ACTION

The IRS agrees with this recommendation. The Chief Financial Officer (CFO) and Chief Technology Officer (CTO) will ensure established test standards and guidelines are adhered to during the conducting of financial systems test efforts, including testing of the Individual Income Tax Credits report and validating Advanced PTC (APTC) and PTC reconciliation reporting. The IRS CTO will ensure adherence to these standards and guidelines through increased monitoring and discussion during regular progress meetings and by employing more frequent written reminders. Any additional testing is contingent on additional resources or the re-prioritization of current workload.

IMPLEMENTATION DATE

January 31, 2017

RESPONSIBLE OFFICIAL

Associate Chief Information Officer for Enterprise Services

RECOMMENDATION 2

The CFO and ACA Project Management Office should work with the CMS to jointly develop procedures for the periodic financial reconciliation of APTC information.

CORRECTIVE ACTION

The IRS agrees with this recommendation. On a quarterly basis, the IRS will reconcile the Exchange Periodic Data (EPD) data to the CMS disbursements paid to the marketplace insurance companies. These reconciliations will be prepared at a summary level and IRS will work with CMS to evaluate any significant variances.

IMPLEMENTATION DATE

May 31, 2016

RESPONSIBLE OFFICIAL

Deputy Associate Chief Financial Officer for Financial Management