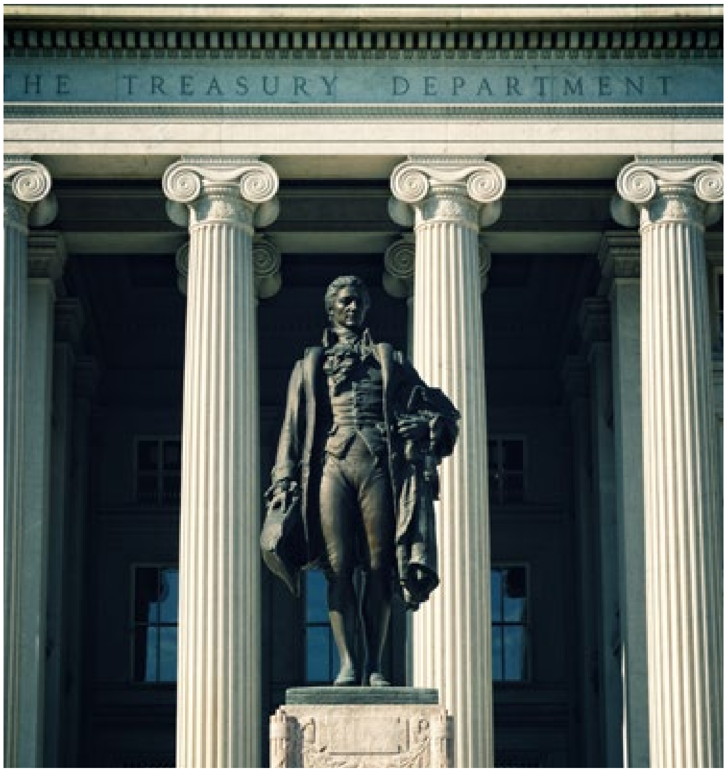
Affordable Care Act

Treasury Inspector General releases assessment on IRS implementation of employer shared responsibility provisions

IRS moving forward with the assessment of employer shared responsibility payments this year

On April 7, the Treasury Inspector General for Tax Administration (TIGTA) released the findings of an audit that was completed to assess the status of preparations by the Internal Revenue Service (IRS) to confirm compliance with the employer shared responsibility provisions. While the TIGTA assessment indicates that the IRS may have fallen behind schedule in its activities to enforce the employer shared responsibility provisions and its administration of the processes may not be as efficient as taxpayers would hope, the primary implication to be drawn from the report is that compliance with the employer shared responsibility provisions remains a key focus and progress toward an organized and accurate enforcement of these provisions is still being pursued by the IRS.



Background

The Patient Protection and Affordable Care Act of 2010 and the Health Care and Education Reconciliation Act of 2010 (the ACA) include the employer shared responsibility provisions. The employer shared responsibility provisions apply to employers that had an average of 50 or more full-time employees, including full-time equivalent employees, during the prior calendar year. These employers are referred to as applicable large employers (ALEs). Under the provisions, ALEs must offer health insurance to full-time employees (and their dependents) during the current calendar year through an employer-sponsored plan beginning in January 2015, or a shared responsibility payment may apply.

The IRS is charged with assessing ALEs with shared responsibility payments based on processing data it receives from numerous sources, including the information reporting initiated by the ACA under Internal Revenue Code Sections 6055 and 6056. To implement these requirements, the IRS developed Forms 1094-C and 1095-C for ALEs to provide information to the IRS about their employees who received offers of coverage from each (ALE) and those who received coverage from the ALEs. The report presents the TIGTA's assessment of the IRS's preparation for validating compliance with the employer shared responsibility provisions of the ACA and the related information reporting requirements.

TITGA Findings

Provided below is a summary of the main findings from the TIGTA assessment report.

- Paper returns were not processed by the IRS in a timely or accurate manner. Due to certain programming errors, the IRS was not able to consistently transfer scanned paper forms to the electronic database, causing a significant delay in processing paper returns. The TIGTA submitted three recommendations to improve various aspects of the scanning process to enable better processing of paper returns for the 2017 reporting year. The IRS agreed with each of the recommendations and agreed to develop better procedures.
- When evaluating the ACA Information Returns (AIR) system for the processing of electronic returns, the report highlighted that business rule validations did not always function appropriately. The TIGTA found that errors were both incorrectly generated and not generated when expected. In total, 16 of the 141 business rule validations did not function correctly for the tax year 2015 transmissions due to insufficient testing. The TIGTA recommended that the IRS validate that all error codes and business rule validations have been tested to work as intended prior to the tax year 2016 filing season. The IRS agreed with this recommendation and has confirmed that it completed testing in December 2016 to enable proper functionality.
- For tax year 2015, the error codes that were returned to filers did not provide enough description for employers to be able to identify and make appropriate corrections. For example, taxpayer identification number (TIN) validation errors only referenced the specific form that caused the error but did not identify the specific TIN on the form that generated the error. The IRS agreed with the recommendation that error codes need to provide sufficient detail for employers to identify and correct such errors. Enhancements were made in January 2017 to provide the applicable information within the acknowledgment files.
- Currently, IRS instructions require errors to be corrected as soon as possible once found. The TIGTA recommended that the IRS establish a required time frame to correct errors received as the IRS's instructions could have various meanings among employers. This was the only recommendation with which the IRS disagreed, commenting that a required correction time frame may go beyond existing regulations and written guidance. The IRS commented

that it will re-evaluate the need to offer such guidance in the future should data indicate increasing penalty application and that it will consider the applicability of good-faith effort in future years.

- Lastly, compliance systems that were intended to identify and enforce employer shared responsibility compliance have been delayed or canceled altogether – with new compliance automation tools underway:
  - First, the implementation of the ACA Compliance Validation (ACV) system, which is intended to identify potentially noncompliant ALEs and calculate the proposed employer shared responsibility payments under § 4980H(a) is delayed by two months to May 2017. Section 4980H(a) relates to the shared responsibility payment that is charged to an ALE that fails to provide offers of coverage to at least 95% (70% for 2015) of its full-time employees.
  - Second, the IRS abandoned efforts to extend the ACV system to identify ALEs who were non-filers or who would be subject to the employer shared responsibility payments under § 4980H(b), instead replacing it with an automation tool. Section 4980H(b) relates to the payment that an ALE must pay if one of its full-time employees qualifies for a premium tax credit for coverage received from the marketplace because the employer failed to offer coverage that met minimum value requirements or because the coverage offered was not affordable to the employee.
  - Finally, the ACA Case Management system that would provide support for the creation, management and status tracking of the § 4980H(a) payments has been canceled altogether in an effort to save funds. The functionality of the ACA Case Management system is being transferred to the development of a broader enterprise case management system. ACA shared responsibility payments will be managed under existing systems until the new enterprise case management system is developed.

Implications

Given filers' experiences with tax year 2015 ACA filings, the findings in the report are largely unsurprising. These are the key takeaways from the audit to keep in mind moving forward:

- Many of the recommendations that involve improvements to the AIR system have already been implemented and have resulted in a much smoother filing season for tax year 2016. For example, the IRS is now using a covered individual ID to indicate the specific individual generating a TIN validation error. This update enables employers to correct their data where needed and potentially mitigate future penalties when "good-faith effort" rules may not be in force.
- The report describes the IRS's reticence to issuing additional guidance around the time frame for employers to correct errors identified on Forms 1094-C and 1095-C. In rejecting the recommendation, the IRS indicates in its response that it prefers to rely on the standard contained in its instructions to those forms that state errors should be corrected as soon as possible after detection. The IRS countered the recommendation by stating a fixed deadline for correction would treat the ACA returns differently from other information returns.
- The IRS previously stated that it expected to begin delivering letters notifying employers of potential liability for shared responsibility payments relating to the 2015 tax year in early 2017. This timeline has been reiterated in an IRS frequently asked question (FAQ) updated on its website as recently as April 6. However, the delay in the implementation of the ACV system until May 2017 and the development of other automation tools mean that employers will not receive these letters until at least May 2017.
- With the cancellation of the ACA Case Management system and expected transfer to another system, it remains unknown what appeals processes will be in place for these penalties or how quickly and effectively the IRS will be able to process employer responses to the letters informing ALEs of their potential liability.

In summary, it would be a mistake for employers not to be ready to respond to letters from the IRS in attempts to enforce the employer shared responsibility payments. The IRS updated its website as recently as April 20, 2017, indicating that it will be sending letters informing ALEs that filed Forms 1094-C and 1095-C for 2015 of their potential liability for an employer shared responsibility payment in 2017. (This was updated from the earlier version of the FAQ, which stated that those letters would be sent in early 2017.) Despite the uncertainties about the future of the employer shared responsibility provision A, the IRS enforcement activity appears to be proceeding. So ALEs should be prepared and be ready to work on review and appeals of any letters from the IRS regarding potential liability.

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For more information, please contact one of the Ernst & Young LLP Workforce Advisory Services professionals below.

Ann Bradshaw
ann.bradshaw@ey.com
+1 713 750 4953

Leigh Messina
leigh.messina@ey.com
+1 214 756 1032

Ali Master
ali.master@ey.com
+1 214 756 1031

Contact us at **eyworkforceadvisoryservices@ey.com**.

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SCORE No. 03062-171US
CSG No. 1704-2270291
ED None

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