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Getting Over the Goal Line: Congress Shows Strong Support for Medical Device Tax Repeal, but Issues Remain

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Introduction

The Patient Protection and Affordable Care Act (“ACA”) generates very few areas of agreement. However, in recent months, proposals to repeal one of the most visible and controversial provisions of the law—the medical device excise tax (“MDET”)—have gained significant momentum.

This alert provides an update on the state of play in Congress with respect to the MDET, including the prospects for repealing the tax this year.

Background

The ACA imposes a 2.3 percent excise tax on domestic sales of medical devices by manufacturers, producers, and importers.¹ This 2.3 percent tax is levied on the medical device manufacturer or importer before a taxable medical device is sent to the wholesaler or hospital. Thus, manufacturers and importers have to pay the tax regardless of whether they make a profit.

A taxable medical device closely tracks the definition of a medical device in the Federal Food, Drug, and Cosmetic Act. However, eyeglasses, contact lenses, hearing aids, and other medical devices sold at retail for individual use are exempt from the MDET, which went into effect on January 1, 2013. In December 2012, the IRS issued final regulations and interim guidance implementing the MDET.²

State of Play

Critics say that the MDET will stifle economic growth by suppressing research and development and preventing U.S. medical device companies from expanding. Moreover, critics charge that the MDET will have a disproportionate effect on small- to medium-size businesses creating innovative new products. By discouraging these companies from investing in R&D costs and bringing new developments to market, the MDET may encourage offshore development of medical devices. Further, hospitals, health care providers who purchase medical devices, and health care supply chain companies are concerned that manufacturers and importers will pass on the cost of the MDET.

While supporters argue that higher demand for medical devices as a result of the ACA will offset the effect of the new tax, the idea of repealing MDET has been steadily gaining momentum in Congress on both sides of the aisle. In fact, both the House and Senate have taken action towards repealing the MDET in recent months.

In March, the Senate voted in favor of repealing the MDET by an overwhelming margin of 79-20 as part of its Fiscal Year 2014 budget resolution. Although the budget resolution is not law and therefore is not binding, the Senate’s vote was not only symbolic but also sent a strong signal that there is bipartisan support to repeal the MDET.



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The House has also signaled its strong support for repealing the MDET. Lawmakers have introduced numerous bills to repeal the tax, including the Protect Medical Innovation Act of 2013 (H.R. 523), which Rep. Erik Paulsen (R-MN) introduced in February of this year. The bill currently has 243 cosponsors, more than the majority needed for passage. Indeed, the House voted to repeal the MDET in the previous Congress.

Why the Holdup?

With strong support in both the House and Senate, it appears that legislation repealing the MDET is primed for passage. However, there are several reasons why the MDET remains in place.

1. **The search for a pay-for.** The cost of repealing the MDET is about \$29 billion over 10 years, according to the most recent estimate from the Joint Committee on Taxation.³ In an era of tight budgets and “pay as you go” policymaking, lawmakers generally have to find a way to pay for proposals that cost money. However, Congress has not yet come to an agreement on how to pay for repealing the MDET. Further, Congress is currently saving revenue in preparation for tax reform; as a result, lawmakers are reluctant to use revenue-raising measures on smaller, standalone measures like repealing the MDET.
2. **Constitutional issues and House dynamics.** The Origination Clause of the U.S. Constitution states that all revenue measures must originate in the House. Although the House strongly supports repealing the MDET, House leadership has imposed a freeze on sending any revenue measures to the Senate at this time. The reason for this policy is that the Senate can take a House revenue measure, strip out the House proposals, and insert its own proposals. Moreover, the Senate’s revenue proposals can be unrelated to the House’s proposals as long as they are in the House’s legislative “shell.” With Ways and Means Committee Chairman Dave Camp (R-MI) making a strong push for comprehensive tax reform, the House does not want to give the Senate an additional opportunity to make statements about tax policy.
3. **Debt ceiling politics.** The federal government is expected to reach its statutory debt ceiling later this year—likely in the early fall. The House may intend to use repeal of the MDET as leverage before they agree to any increase in the debt limit. As the House and Senate continue to formulate their strategies with respect to the debt ceiling, repealing the MDET may be one of many scenarios under discussion. Although Administration officials are adamant that raising the debt ceiling is not negotiable, strong support for repealing the MDET may apply sufficient pressure to include the proposal as part of a debt ceiling package.

Getting Over the Goal Line

The path forward for MDET repeal in Congress remains somewhat unclear. In the meantime, medical device manufacturers and importers are faced with figuring out how to implement the MDET. The IRS has issued final regulations that taxpayers must interpret but has reserved judgment on other aspects of the statute, leaving stakeholders with uncertainty going forward. Deciding whether you fit into one of the excepted categories in the statute and regulations could make a significant difference in a company’s ability to compete and affect the availability of cash to invest in research and development.

The MDET has the potential to significantly impact the bottom lines of medical device manufacturers, producers, and importers, as well as health care providers, health care supply chain companies, and others. Given the uncertainty surrounding the MDET, businesses should determine their compliance with the tax and the extent to which the MDET may impact their operations moving forward.

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Additionally, stakeholders are encouraged to make their voices heard among lawmakers. Although repealing the MDET appears to be one of the few areas of agreement in Washington with respect to health care, the issue is not over the goal line yet.

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¹ The MDET was included in the Health Care and Education Reconciliation Act of 2010, which amended the ACA. *See* P.L. 111-152, Title I, Subtitle E, § 1405(a)(1), 124 Stat. 1029, (2010) (amending the Patient Protection and Affordable Care Act of 2010, P.L. 111-148).

² T.D. 9604, 2012-52 I.R.B. 730; I.R.S. Notice 2012-77, 2012-52 I.R.B. 781.

³ JOINT COMMITTEE ON TAXATION, DESCRIPTION OF H.R. 436, THE “PROTECT MEDICAL INNOVATION ACT OF 2011,” JCX-45-12 (May 29, 2012), *available at* <https://www.jct.gov/publications.html?func=startdown&id=4431>.