House Committee on Ways and Means, Health Subcommittee

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I have been invited by the Subcommittee staff to provide testimony regarding the following question: whether income-qualified persons who purchase medical insurance on exchanges operated by the federal government under Section 1321 of the Patient Protection and Affordable Care Act (Affordable Care Act or ACA), may receive the same subsidies to which those persons would be entitled if they purchased medical insurance on an exchange operated by the state or on the state's behalf by a non-profit organization under Section 1311 of the ACA, even as the Internal Revenue Service has so provided in rules it has promulgated under the ACA.

This is an issue that I have helped flag about a year ago.[1] But while I have had a not insubstantial role in giving birth to the issue, the matter has truly been raised to analytical maturity by Jonathan Adler of Case Western law school and Michael Cannon of the Cato Institute. Their working paper, "Taxation Without Representation: The Illegal IRS Rule to Expand Tax Credits under the PPACA,"[2] reflects a thoughtful and comprehensive analysis of the issue. In my testimony, I cannot hope to cover the issues in the comprehensive and nuanced way that Adler and Cannon do, and I commend those who seek further insights on the matter to consult the Adler and Cannon working paper. My goal is more modest – to provide a thumbnail of the issue and an accessible Baedeker to the concerns that serious analysts must have about the way that the IRS, in broad rulemaking on the exchanges provided for under the ACA, has likely exceeded its authority under the ACA.

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[1] http://www.investors.com/NewsAndAnalysis/Article/584085/201109071840/ObamaCare-Subsidy-Error-Found.htm; http://www.investors.com/NewsAndAnalysis/Article/585053/201109161746/ObamaCare-Goof-On-Firm-Fines-.htm

[2] Case Research Paper Series in Legal Studies, Working Paper 2012-29 (July 2012).

I very much appreciate the invitation of the Subcommittee to appear before it and the opportunity I have been given to share some thoughts on this important matter – a critical matter as a number of states have reported that they do not plan to establish exchanges, with the result that federally-run exchanges will likely be more prevalent than once thought. In the comments I make in this testimony and in my in-person appearance before the Subcommittee, I speak as an individual, not as a representative of Vanderbilt University or any other institution.

The issue affects opportunity for subsidy by residents of states that choose not to establish an exchange under Section 1311 of the ACA, and it affects (large) employers, which face liability if even one employee receives federal subsidy for the purchase of medical insurance on an exchange. The issue also affects significant institutional interests. For example, its resolution implicates state autonomy – states' roles as gatekeepers of federal subsidies and their ability to strike the appropriate balance between (i) providing access to federal subsidies for their residents who have incomes that qualify for federal subsidies and for (ii) providing a safe harbor (and competitive advantage) for their employers who face taxes/penalties if their employees secure federal subsidies. The issue also bears, importantly, on the relationship between a federal agency (the IRS) and (i) the prerogative of Congress to provide for and define the scope of benefits for citizens and (ii) the prerogative of Congress to levy taxes/penalties and determine the scope and incidence of such levies.

Federal agencies operate on the basis of delegated authority from Congress, and within the scope of such authority their actions receive appropriate deference. But in the process of determining the scope of that authority, the statutory framework governs.

I. The Provisions of the ACA

The ACA's relevant provisions are rather straight forward on the issue. The ACA makes provision for two types of exchanges where persons may purchase medical insurance and where health insurance companies compete with each other. Section 1311 provides for states to establish such an exchange. The language seems mandatory (states "shall" establish such an exchange), but Section 1321 softens the mandatory quality of Section 1311 by providing that the federal government must ("shall") set up a federally run exchange where states do not set up such an exchange. Section 1321 undoubtedly is a recognition that the federal government cannot, under the anti-commandeering principle, compel states to establish an exchange.[3]

[3] Printz v. United States, 521 U.S. 898 (1997); New York v. United States, 505 U.S. 144 (1992). See generally, James F. Blumstein, *Enforcing Limits on the Affordable Care Act's Mandated Medicaid Expansion: The Coercion Principle and the Clear Notice Rule*, CATO SUPREME COURT REVIEW (forthcoming September 2012).

Under the ACA's terms (Section 1401), subsidies are established for persons who are enrolled in a qualified health insurance plan through an exchange that is (a) established by a state and (b) established by a state pursuant to its authority under Section 1311. Both descriptive and limiting terms [(a) and (b)] are expressly enumerated in Section 1401.

No comparable subsidy provision exists in the ACA for persons who are analogously enrolled in a qualified health insurance plan through an exchange that is (a) established by the federal government and (b) established pursuant to Section 1321. Two types of exchanges are contemplated, but, under Section 1401 of the ACA only one provides access to federal subsidies – the one established by states under Section 1311.

Under the familiar canon of statutory construction, *expressio unius est exclusio alterius*, the expression of one thing is the exclusion of another (of the same kind). That is, where a written instrument, such as a contract or a statute, by its express terms includes one or more things of a class, it simultaneously implies the exclusion of the balance of that class. Under this canon of statutory construction, the ACA's granting of subsidies for income-qualified enrollees under state exchanges established under Section 1311 is to be construed not to grant comparable subsidies for income-qualified enrollees under federal exchanges established under Section 1321.

If one examines the ACA by itself, the *expressio unius* canon of construction would very likely end the analysis, absent some very strong reason for a court to reason otherwise. As Adler and Cannon carefully and clearly establish, there are no strong reasons for a court not to accept the plain language of the ACA about the scope of federal subsidies available.

II. The IRS Rule

Despite the clear distinction between federally run exchanges under ACA Section 1321 and state run exchanges under ACA Section 1311, the IRS has issued a rule that provides for federal subsidies for income-qualified persons who are enrolled in either a state run or a federally run exchange. The question is whether the IRS rule is sustainable in light of its substantial expansion of the scope of federal subsidy described in the plain language of the text of the ACA.

The IRS' rule was promulgated in the context of rulemaking, and it is to be applauded procedurally in that regard. Rulemaking is a preferable process to informal regulatory guidances, which have been used in other contexts in the implementation of the ACA. Such informal procedures are not subject to notice and comment and are not typically reviewable as part of executive regulatory review through the Office of Information and Regulatory Affairs at the Office of Management and Budget. The problem with the IRS rule is not procedural but substantive.

Under the ACA, large employers (more than fifty employees) are required to offer their employees health insurance that is affordable and that meets federal minimum coverage/benefits

standards. If large employers do not offer qualifying health insurance coverage for their employees, they face liability in the form of a substantial per-employee tax/penalty. The tax/penalty is triggered if a single employee receives a health insurance premium credit on an exchange established by the state under Section 1311. The ACA makes no mention of triggering the employer tax/penalty if one of the employer's employees receives a health insurance tax credit on a federally run exchange under Section 1321.

By extending the health insurance premium tax credit to income-qualified persons enrolled in federally run exchanges, the IRS rule triggers liability for employers in states that have federally run exchanges and for employers who have at least one employee enrolled and receiving premium tax credits in a federally run exchange. By itself, the ACA only imposes such employer liability when a large employer does not provide qualifying health insurance and when an income-qualified employee receives a health insurance premium tax credit through a state run exchange under Section 1311.

So, the IRS rule on this issue is a double-edged sword. It expands benefits to income-qualified employees in states that choose not to set up exchanges (and therefore have federally run exchanges). At the same time, the rule triggers potentially substantial taxes/penalties to employers whose employees receive the expanded IRS-driven benefits. Can the IRS add benefits and impose costly sanctions in this way – beyond the authorization in the ACA itself?[4]

At the outset, one should recognize that specific statutory terms are often adopted by an administering agency, even if the terms appear odd. *United States v. Locke*[5] is a good example. Congress in that case specified a filing deadline of December 30, even though it was customary for a deadline to track the end of a month, and December has thirty-one days. Despite the risk of confusion, which triggered the litigation, the agency adopted the December 30 deadline, not extending it to December 31. It respected the Congressional will as reflected in the text of the statute, not taking it upon itself to undo and redo the straight forward textual command. Speaking for the Court, Justice Marshall upheld the December 30 date.

In the case of the exchange subsidy rule, the IRS is moving out on its own with little authority derived from the statute itself. Adler and Cannon present evidence that the legislative history supports a claim that the decision to vest gatekeeping power with states was purposeful – an incentive for states to establish exchanges, which the federal government desired but could

[4] It does not appear that the IRS actually claims express statutory authority for this component of its rule. It seems to assert only that the rule is consistent with the ACA, but that is only true if the IRS disrespects the *exclusio unius* canon of construction and treats the plain language as not reflecting a plausible or coherent statutory policy. The legislative text is traditionally the most reliable indicator of legislative meaning and intent. See note 12, *infra*.

[5] 471 U.S. 84 (1985)(per Justice Marshall).

not command (despite the "shall" language in Section 1311). After a phase-in period, states are responsible for paying for (and raising revenue to pay for) the operation of state-run exchanges. The cost of operating federal exchanges must be borne by the federal government.

But whether or not this distinction between exchanges was purposeful, there is surely a plausible argument that the distinction serves valid federalism and state autonomy goals. Under the statutory terms of the ACA, states choose the proper balance between access to subsidies for medical insurance for its residents, on the one hand, and competitive advantage for its businesses, on the other hand (typically an important part of attracting or retaining employers to a state and an important part of job creation in a state).

In addition, there is a concern that the IRS not be permitted to impose taxes or penalties when such sanctions have little or no basis in statutory law. At a minimum, the statute should contemplate an agency role in filling in a gap; but nothing in the ACA seems to contemplate such a role for the IRS on this specific issue. In short, given the ACA's provisions on the exchange subsidy issue, there is no evidence that Congress contemplated that there was a gap to fill here. And such a finding is a threshold requirement in order to authorize agency action like that of the IRS and, correlatively, to invoke norms of deference to agency decisionmaking.

The ACA authorizes the IRS to promulgate regulations to implement the terms of the statute. So, the authority of the IRS to engage in ACA rulemaking is not subject to question, as a general matter.

But agency authority exists only to resolve or fill gaps regarding legislative ambiguity. And then, the agency can act to clarify but only within the scope of the ambiguity.[6] Where statutory language is unambiguous, as it is here with the ACA, "Congress did *not* delegate gap-filling authority to an agency."[7] And the question of ambiguity relates not in the abstract but to a "particular issue"[8] and a particular "context."[9] Traditional tools of statutory construction are to be used in determining whether ambiguity (and thereby gap-filling authority) exists regarding "the precise question at issue."[10] So the *expressio unius* canon of statutory construction is critical here in understanding the limitations on IRS gap-filling authority.

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[6] United States v. Home Concrete & Supply, LLC, 132 S. Ct. 1839, 1848 (2012) (Scalia, J., concurring).

[7] *Id.* at 1843 (plurality opinion of Breyer, J.)(emphasis in original).

[8] *Id.*

[9] FDA v. Brown & Wiliamson Tobacco Corp., 529 U.S. 120, 132-33 (2000).

[10] Home Concrete, 132 S. Ct. at 1844. (internal cite and quote omitted).

It is one thing for the IRS to adopt a rule about the details of how the exchanges will work. That task was given to the agency. It is quite another to assume that the agency has power to define what the ACA has already unambiguously defined under the *expressio unius* doctrine – namely, which exchange(s) qualify for federal subsidies. On that question, there is no ambiguity.[11] Subsidies are provided for on one type of exchange – state run exchanges under Section 1311. Under the traditional canon of *expressio unius*, one should infer no ambiguity regarding the absence of provision for subsidy for those enrolled in federally run exchanges under Section 1321.[12] And in the absence of ambiguity, the justification for the IRS rule vanishes, since agency gap-filling authority is absent when a particular component of a "statute is unambiguous," and therefore "there is no gap for the agency to fill" and "thus 'no room for agency discretion.'"[13] Under *expressio unius* principles, Congress has not delegated to the IRS "the power to fill a gap"[14] on the question of whether a federally run exchange under Section 1321 can serve as a vehicle for a federal subsidy and thereby a tax/penalty on a large employer. For these reasons, the IRS rule in question is likely beyond the agency's delegated power under the rule in question.

An argument has been made that a reconciliation bill passed as part of the ACA enactment process authorizes the IRS' rule in question.

The reconciliation bill imposed an obligation on both federally run and state run exchanges to report information "regarding tax credits provided to individuals."[15] This set of reporting requirements, applicable to both federally run and state run exchanges, purports to show that "Congress demonstrated its understanding that federal exchanges would administer premium tax credits."[16]

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[11] Cf. Cuomo v. The Clearing House Assn., LLC, 557 U.S. 19, 525 (2009)(Federal agency "can give authoritative meaning to the statute within the bounds of that uncertainty. But the presence of some uncertainty does not expand *Chevron* deference to cover virtually any interpretation" of the statute involved).

[12] As the Supreme Court has stated, "[t]here is... no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes." Griffin v. Oceanic Contractors, 458 U.S. 564, 571 (1982).

[13] Home Concrete, 132 S. Ct. at 1843 (plurality opinion of Breyer, J.).

[14] *Id.* (internal quote and cite omitted).

[15] Timothy S. Jost, *Yes, the Federal Exchange Can Offer Premium Tax Credits*, HEALTH REFORM WATCH, Sept.11, 2011, http://www.healthreformwatch.com/2011/09/11/yes-the-federal-exchange-can-offer-premium-tax-credits/.

[16] *Id.*

This reporting requirement does not change any substantive provision of the ACA. At most it demonstrates a misunderstanding of the provisions of the ACA. It does not demonstrate any ambiguity in the text of the statute, and it does not indicate anything about a policy preference for subsidies to apply to both federally run and state run exchanges. The reporting requirement does not affirm the desirability of any change in the ACA. All it shows is that the House drafters of the reconciliation legislation, in the heat of the moment, did not understand the provisions of the Senate-drafted ACA. This type of misunderstanding does not and cannot alter the substantive terms of the underlying provisions of the ACA, nor can it serve to justify a *post hoc* expansion of administrative power to expand federal subsidies and, correlatively, impose monetary penalties or taxes on employers. Nor can it justify the loss of state autonomy in states' roles as gatekeepers of federal subsidies, a loss of state authority that should be achieved under a much clearer legislative mandate.[17] The reporting requirement of the reconciliation legislation is not a substantive provision and effects no substantive change in the ACA. It cannot and does not provide administrative authority to fill a gap that does not exist in the terms and provisions of the ACA.

III. Conclusion

The ACA contemplates two forms of health insurance exchange – one run by states under Section 1311, the other run by the federal government under Section 1321. The ACA provides for tax credits (subsidies) for income-qualified persons enrolled in plans through a state run exchange under Section 1311. The statutory provision specifically enumerates the state as administrator (itself or through a non-profit agency) and also specifically enumerates the statutory section that provides states authority to set up an exchange. There is no comparable provision for subsidy for federally run exchanges. The listing of one exchange for subsidy and the omission of the other exchange means, under the *exclusio unius* canon of statutory construction, that the statutory design excludes enrollees on federally run exchanges from receiving subsidies for the purchase of health insurance.

The addition of subsidies for those income-qualified enrollees on federally run exchanges triggers a tax/penalty for large employers that do not provide qualified health insurance to their employees. Under the ACA, the employer tax/penalty accrues when an income-qualified employee of such a large employer receives a federal subsidy on a state run exchange. The IRS rule extends this financial exposure to employers in states that do not choose to set up an exchange. This extends the power of taxation and monetary sanctions to the IRS in ways not contemplated by the terms of the ACA itself.

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[17] Cf. Gregory v. Ashcroft, 501 U.S. 452 (1991).

Under the circumstances, there would seem to be no ambiguity and therefore no gap-filling power for the IRS on this specific issue. If this legislative change is to be made, then, it should be done by Congress. And the fact that there has been a significant change in the legislative balance of power in Congress is, if anything, a stronger case against the IRS rule since it reflects administrative supersession of a legislative prerogative and a dubious shift in power to the executive branch from the legislative branch.