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HEALTH REFORM LAW MAKES CLEAR THAT SUBSIDIES WILL BE AVAILABLE IN STATES WITH FEDERALLY OPERATED EXCHANGES

By Judith Solomon

Some health reform opponents claim that the Affordable Care Act's (ACA) premium tax credits to help low- and moderate-income uninsured people buy coverage through the new health insurance exchanges are *only* available in states that have set up their own exchanges, not in states with federally operated exchanges. A group of Republican members of Congress led by Representative Michele Bachmann (R-MN) and Senator Jim DeMint (R-SC) have urged governors to forgo establishing their own exchanges on this ground in order to undermine ACA implementation and thus assist their efforts to repeal health reform.[1]

The argument that premium credits are not available to purchase coverage offered through a federally operated exchange rests on a distorted and incorrect reading of the ACA.

- Section 1321 of the ACA says that if a state elects not to establish its own exchange or will not be ready to operate its exchange in 2014, "the Secretary shall (directly or through agreement with a not-for-profit entity) establish and operate *such* Exchange within the State and the Secretary shall take such actions as are necessary to implement such other requirements" (emphasis added).[2] In other words, *the federal government will stand in the shoes of a state that elects not to operate an exchange by establishing and operating the exchange on the state's behalf.*[3]

- Section 36B of the Internal Revenue Code, which was added to the Code by section 1401 of the ACA, specifically refers to federal exchanges in requiring *all* exchanges — state and federally operated — to report to the federal government on the amount of advance payments of premium credits that taxpayers receive. That provision would make absolutely no sense if people purchasing coverage through a federally operated exchange were not eligible for the credits.

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[1] Letter to National Governors Association, June 29, 2012, http://bachmann.house.gov/uploadedfiles/congresslettertonga_062912.pdf.

[2] Section 1321(c) of the Affordable Care Act.

[3] A new report claiming that premium credits are *not* available in federally run exchanges ignores section 1321's direction to the Secretary to "establish and operate such exchange within the State." This language makes it clear that the federal exchange *is* the state exchange in states that elect not to establish and operate their own exchanges. Jonathan H. Adler and Michael F. Cannon, "Taxation Without Representation: The Illegal IRS Rule to Expand Tax Credits under the PPACA," Case Research Paper Series in Legal Studies, Working Paper 2012-17, July 2012.

- If premium credits were not available in states with federally operated exchanges, residents of such states would not qualify for help buying coverage in the exchange, while residents of states establishing their own exchanges would qualify. This would clearly be inconsistent with the purpose of the health reform law, which is to ensure that all Americans have a path to affordable coverage regardless of where they live. As Chief Justice Roberts noted in referring to the ACA's Medicaid expansion, the exchanges are "an element of a comprehensive national plan to provide universal health insurance coverage."[4]

- The Treasury Department has specifically rejected the argument that people buying coverage through a federally operated exchange are not eligible for premium credits. A court considering this question would almost certainly defer to the Treasury interpretation.

Federal Exchange *Is* the State Exchange in States Not Establishing Their Own Exchange

Section 1311 of the ACA calls for states to establish health insurance exchanges to serve as marketplaces for individuals and small businesses to purchase health coverage. So far, 34 states and the District of Columbia have received federal grants to establish exchanges.[5]

To make health insurance more affordable for low- and moderate-income people, the ACA provides that citizens and legal immigrants with incomes between 100 and 400 percent of the poverty line who are not eligible for Medicaid or Medicare and don't have an offer of employer coverage can receive premium tax credits to help them buy insurance offered in the exchange. The premium tax credits are payable in advance on a monthly basis directly to insurers. At the end of the year, the IRS determines the final premium tax credit for which a household qualified, based on its annual income.[6]

Exchanges will determine whether people are eligible for advance payments of the credit and the amount of the monthly payment to their health plan. Those who are eligible can receive help paying premiums in "coverage months" during which they are enrolled in health plans offered in an exchange. A month is a "coverage month" if a taxpayer, spouse, or dependent was enrolled that month in a plan "through an Exchange established by the State."[7]

Not all states will set up their own exchanges. Although states have until November to declare their intent to establish an exchange, several governors have already said they will not establish an exchange.[8]

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[4] *National Federation of Independent Business v. Sebelius,* Opinion of Chief Justice Roberts at pages 53-54.

[5] "Status of State Health Insurance Exchange Implementation," Center on Budget and Policy Priorities, updated June 5, 2012, http://www.cbpp.org/files/CBPP-Analysis-on-the-Status-of-State-Exchange-Implementation.pdf.

[6] The eligibility requirements for premium tax credits are in section 36B of the Internal Revenue Code

[7] Section 36B(c)(2) of the Internal Revenue Code.

[8] *Ibid.* For example, the governors of Texas, Louisiana, and Maine have declared that they will not establish an exchange.

Congress anticipated that some states would forgo setting up their own exchange or might not be ready to begin operations on January 1, 2014 as required. The ACA thus includes a fallback so that all eligible people can have access to affordable coverage, regardless of where they live. Under section 1321 of the ACA, if a state elects not to establish its own exchange or will not be ready to operate its exchange in 2014, "the Secretary shall (directly or through agreement with a not-for-profit entity) establish and operate such Exchange within the State and the Secretary shall take such actions as are necessary to implement such other requirements."[9]

In other words, if a state elects not to operate an exchange, the federal government will establish and operate the exchange on the state's behalf.

Despite this language directing the Secretary to establish "such Exchange within the State" and to take actions necessary to implement "such other requirements," critics of health reform have seized on the reference in section 36B of the Internal Revenue Code to an exchange "established by the State" in the definition of a coverage month. This reference, they contend, means that individuals in states with a federal exchange cannot qualify for premium tax credits.[10]

However, the Treasury Department flatly rejected this claim when it adopted final regulations to implement the ACA, explaining that the ACA's legislative history, structure, and purpose all make clear that premium tax credits are available to taxpayers who obtain coverage in a federally operated exchange:

> The statutory language of section 36B and other provisions of the Affordable Care Act support the interpretation that credits are available to taxpayers who obtain coverage through a State Exchange, regional Exchange, subsidiary Exchange, and the Federally-facilitated Exchange. Moreover, the relevant legislative history does not demonstrate that Congress intended to limit the premium tax credits to State Exchanges. Accordingly, the final regulations maintain the rule in the proposed regulations because it is consistent with the language, purpose, and structure of section 36B and the Affordable Care Act as a whole.[11]

Not only does section 1321 indicate that a federally operated exchange *is* the exchange established by the state in a state electing not to operate its own exchange directly, but section 36B of the Internal Revenue Code specifically refers to federal exchanges in requiring *all* exchanges — state and federally operated — to report to the federal government on the amount of advance payments of premium credits that taxpayers receive. That provision would make no sense if people purchasing coverage through a federally operated exchange weren't eligible for the credits and clearly demonstrates Congressional intent that the tax credits be available in all states regardless of which level of government is operating the exchange.

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[9] Section 1321(c) of the Affordable Care Act.

[10] See for example, Jonathan Adler and Michael Cannon, "If ObamaCare survives, legal battle has just begun," *USA Today*, June 25, 2012.

[11] *Federal Register,* Vol. 77, May 23, 2012, at page 30378. Regulations setting out the standards for exchanges issued by the Department of Health and Human Services (HHS) define the term exchanges to include "State Exchanges, regional Exchanges, subsidiary Exchanges, and a Federally-facilitated Exchange." 45 CFR §155.20.

Even if section 36B did not include federally operated exchanges in its discussion of premium credits, the argument limiting the payment of credits to state exchanges would still lack credibility because it ignores the ACA's overall design and structure. If premium tax credits were not available in states with a federal exchange, low- and moderate-income residents of Louisiana, Texas, Maine, and other states would receive no help buying health coverage, while residents of Colorado, Nevada, Maryland, and other states establishing their own exchanges would receive assistance. This would be inconsistent with the purpose of the health reform law, which is to ensure that all Americans have a path to affordable coverage regardless of where they live.

Courts Will Defer to Treasury Department Regulations

Opponents of health reform apparently intend to file a legal challenge to the law on behalf of one or more employers who are penalized for not providing coverage in a state with a federal exchange, based on the claim that the federal exchange was not authorized to provide the subsidies.[12] A court considering such a claim would almost certainly defer to the Treasury Department interpretation that subsidies are fully available through federally operated exchanges.

Courts use a two-step test established by the U.S. Supreme Court in the 1984 case *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc. (Chevron)*.[13] The first step is to determine whether the statutory language is clear or ambiguous. If the language is clear, then the law must be given effect as written. If the law is silent or ambiguous, the court must take the second step of determining whether the agency's interpretation is based on a permissible construction of the statute. In making this determination, the "court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency."[14]

In providing for a federal exchange, Congress clearly intended that it substitute for a state exchange. One of the primary functions of an exchange is to determine eligibility for, and the amount of, advance premium tax credits so that people can afford to buy coverage. The language of section 1321 of the ACA establishing the federal exchange is clear on that point, as is the reference in section 36B of the Internal Revenue Code to credits being provided through a federally operated exchange. But even if the statute were ambiguous, a court examining whether the Treasury regulations are valid would certainly defer to the agency's interpretation of the statute because it is both permissible and reasonable.

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[12] Jonathan H. Adler, "If Health Reform Law Survives, Litigation Will Continue," The Volokh Conspiracy, June 27, 2012 at http://www.volokh.com/2012/06/24/if-health-reform-law-survives-litigation-will-continue/.

[13] 467 U.S. 837 (1984).

[14] *Id.* at 844.