No. 14-1158

IN THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

DAVID KING, et al.,

Appellants,

v.

KATHLEEN SEBELIUS,
SECRETARY OF HEALTH AND HUMAN SERVICES, et al.,

Appellees.

On Appeal from the United States District Court
for the Eastern District of Virginia (No. 13-630-JRS)

BRIEF OF THE STATES OF KANSAS AND NEBRASKA AS *AMICI CURIAE* IN SUPPORT OF REVERSAL

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GLOSSARY

ACA or Act	Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029
Amici States	States of Kansas and Nebraska
HHS	U.S. Department of Health and Human Services
IRS	Internal Revenue Service
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IDENTITY AND INTEREST OF *AMICI CURIAE*

Amici States seek to protect the choice Congress gave them: to either (1) create a state-run marketplace (or "Exchange") for selling qualified health insurance plans under the Patient Protection and Affordable Care Act ("ACA" or "the Act"), with the consequent benefits and burdens under the Act, or (2) opt out of the benefits and burdens associated with establishing a state-run Exchange.[1] In States that opt out, a federally funded premium assistance tax credit is not available to individuals who purchase insurance through the required fallback federal marketplaces. In turn, large employers (including States and their political subdivisions) are not subject to the employer mandate. But the Internal Revenue Service ("IRS") has undermined the States' choice by extending the federal premium assistance subsidy to those States anyway. As a result, the regulations expose otherwise-exempt individuals to the individual mandate and trigger the employer mandate in States—including *amici*—that exercised the choice Congress gave them to avoid these additional regulatory burdens.

The IRS regulations (together, "the IRS Rule" or "the Rule") undo the cooperative federalism structure of the ACA's Exchange provisions by overriding their unambiguous meaning. Not only does the Rule violate the ACA, it unlawfully subjects *Amici* States to the employer mandate and displaces their sovereign

[1] Fed. R. App. P 29(a) authorizes States to "file an amicus-curiae brief without the consent of the parties or leave of court."

authority to promote the welfare of their citizens by pursuing economic and social policies of their choosing.

Amici—the States of Kansas and Nebraska—made a deliberate and reasoned decision not to establish State Exchanges. *Amici* States file this brief to defend their rights under the ACA and the Constitution.

SUMMARY OF ARGUMENT

Notwithstanding its overall labyrinthine complexity, the ACA is strikingly clear on the critical point at issue in this case: the federal subsidy for health insurance is only available through marketplaces, or "Exchanges," that a *State creates*. In turn, the employer mandate only applies in and to States that have chosen to establish their own Exchange. Conversely, the subsidy is not available and the employer mandate does not apply in (or to) States that chose not to establish an Exchange of their own, but instead allowed the federal government to create a fallback Exchange. The text of the ACA is clear, and the natural reading of the statute makes perfect sense in light of Congress' objectives and our system of federalism.

The Exchanges are an important pillar of the ACA; they are the mechanism by which Congress intended many individuals to purchase mandatory health insurance. But Congress wanted the States to establish the marketplaces—not the federal government. Because the Tenth Amendment prohibits Congress from

simply requiring States to adopt or implement federal regulations, Congress had to induce States to set up their own Exchanges. So Congress offered States what it hoped was attractive bait in the form of a refundable tax credit to subsidize premiums for low- and middle-income Americans who purchase health insurance through a state-run Exchange. The subsidy, however, had collateral consequences for States: making the ACA tax credit available would extend the individual mandate to individuals who otherwise would be exempt from it, and would trigger the employer mandate, which requires all large employers in the State (including the States themselves) to provide qualified health insurance to full-time employees.

In the end, 34 States did not take the bait and instead chose not to establish State Exchanges. These States made deliberate and reasoned decisions based on the type of regulatory environment they wanted to provide for individuals and businesses living and operating within their borders. In these States, as a fallback, the ACA required the federal government to establish Federal Exchanges. Under the plain text of the Act, individuals who purchase health insurance on one of these fallback Federal Exchanges are not eligible for the premium assistance subsidy. Indeed, the Act would not make sense if the subsidy was available on Federal Exchanges because that would remove the incentive Congress enacted to encourage States to create their own Exchanges.

The Act is explicit and its meaning inescapable: the federal subsidy for health insurance is limited to policies "enrolled through an Exchange established by the *State*." 26 U.S.C. § 36B(c)(2)(A)(i) (emphasis added). Yet the IRS Rule extends the premium assistance tax credit to *any* Exchange, including the Federal Exchanges in the 34 States that chose the legitimate option of not setting up their own Exchange. The Rule contradicts the plain text of the Act in an apparent effort to rewrite the deal that Congress struck. In so doing, the Rule turns the Exchange provisions on their head.

By allowing the IRS to ignore the clear distinction between state-run Exchanges and federal-government-run Exchanges, the District Court approved the IRS' rewriting of the Act. Thus, the District Court condoned allowing a federal agency to displace States' legitimate decisions to act as "the State" for purposes of setting up an Exchange under the ACA. Put another way, the District Court dispensed with Congress' enacted bait for the States, and instead created a net to capture all of the States. This confounding interpretation of the Act bears no relation to the actual text of the Act, ignores States' separate sovereignty, and rewrites the deal Congress offered the States regarding the benefits and burdens of establishing (or declining to establish) state-run health insurance Exchanges.

The consequences for States are profound. The IRS Rule unilaterally extends the employer and individual mandates to otherwise-exempt employers and

individuals in States with federal exchanges—the very result the ACA gave *Amici* States the option to avoid by declining to establish State Exchanges. Moreover, the Rule violates the Tenth Amendment by imposing coercive penalties (or worse, direct taxes) that interfere with States' sovereign employment decisions.

The District Court conceded that the "plain meaning" of the statute "has a certain common sense appeal." Joint Appendix ("JA") 311. But instead of relying on common sense, taking Congress at its word, and confining the IRS to its statutory authority, the District Court did just the opposite. It turned to an amorphous "congressional intent to ensure broad access of affordable health coverage for all," JA311, a lack of "direct support in the legislative history of the ACA," JA311, and perceived "anomalies" in the operation of other provisions of the Act, JA306-JA310, to override the statute's plain meaning.

The District Court's unprincipled approach (1) contradicts the plain text of the ACA; (2) contradicts the structure of the Act and the purpose of limiting the federal subsidy to State Exchanges; (3) undermines States' deliberate and reasoned decisions not to establish state-run Exchanges; (4) twists the statute to allow the federal government to act as a State for purposes of establishing a health insurance Exchange; and (5) unlawfully imposes the employer mandate on States, displacing States' sovereign discretion to define the terms of employment for government employees. The decision should be reversed.

ARGUMENT

I. The IRS Rule Extends The Premium Assistance Tax Credit To Federal Exchanges In Direct Violation Of The ACA's Unambiguous Text.

The ACA requires that "[e]ach State shall, no later than January 1, 2014, establish an American Health Benefit Exchange" that "facilitates the purchase of qualified health plans." 42 U.S.C. § 18031(b)(1)(A). Conscious that requiring States to establish Exchanges would violate the Tenth Amendment, *see Printz v. United States*, 521 U.S. 898, 935 (1997), Congress gave States the choice to opt out. In States that elected not to establish an Exchange, Congress created fallback federal Exchanges by requiring the U.S. Department of Health and Human Services ("HHS") to "establish and operate such Exchange within the State." 42 U.S.C. § 18041(c).

Although Congress gave States a choice whether to establish a State Exchange under section 18031, or accept the fallback Federal Exchange under section 18041, it clearly wanted States to choose the former. Congress used tried and true incentives—primarily money, and a lot of it—in an attempt to induce States to undertake the costly, complex, and controversial job of establishing health insurance Exchanges. Congress authorized the premium assistance tax credit for low- and middle-income taxpayers to be available only when "the taxpayer is covered by a qualified health plan . . . that was enrolled in through an Exchange

established by the State under [42 U.S.C. § 18031]." 26 U.S.C. § 36B(c)(2)(A)(i) (emphasis added).

The Act is clear: the premium assistance tax credit is exclusively available on an Exchange "established by the State under [Section 18031]," *id.*; the subsidy is not available on Exchanges established by the federal government under Section 18041. Yet the IRS Rule eliminates this statutory distinction; it extends the premium assistance tax credit to anyone "enrolled in one or more qualified health plans through an Exchange." 26 C.F.R. § 1.36B-2(a)(1). It then defines "Exchange" as "a State Exchange, regional Exchange, subsidiary Exchange, and Federally-facilitated Exchange." *Id.* § 1.36B-1(k); 45 C.F.R. § 155.20; *see also* 77 Fed. Reg. 30,377, 30,377-78, 30,387. Even the District Court observed that the "plain meaning . . . of section 36B"—as opposed to the IRS' contorted interpretation—"has a certain common sense appeal." JA311. This should have been "the end of the matter" because "the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 842-43 (1984); *see also* 7 U.S.C. § 706(2); *see also Bracamontes v. Holder*, 675 F.3d 380, 387 (4th Cir. 2012) (an agency "may not make its own administrative amendments" to duly enacted statutes; the Court is "obliged to give effect to the statutes as written and enacted").

II. The IRS Rule Also Contradicts The Structure Of The Act And The Purpose Of Limiting The Premium Assistance Tax Credit To State Exchanges.

Instead of ending with the statutory text and invalidating the unlawful IRS Rule, the District Court turned to one-sided policy rationales and perceived "anomalies" in other provisions of the Act to trump the plain language of the subsidy provision. The District Court's slanted view of the purpose and operation of the Act rewrites the premium assistance tax credit provision according to the Executive Branch's own policy priorities while ignoring the Act's plain text and structure.

The plain language of the premium assistance tax credit provision shows that Congress deliberately limited the subsidy to State Exchanges because it wanted to induce States to set up the Exchanges instead of opting for the fallback Federal Exchanges. Because the Tenth Amendment prohibits Congress from requiring States to implement and enforce federal regulations, Congress had to use other tools to persuade the States. *See New York v. United States*, 505 U.S. 144, 166-69 (1992); *see also South Dakota v. Dole*, 483 U.S. 203 (1987) (upholding a federal law that withheld a portion of highway funds from States that set their legal drinking age lower than 21 years old).

Congress has routinely—and effectively—used the promise of federal funding (or the threat of ending it) to spur States to congressionally-desired action.

See, e.g., 42 U.S.C. §§ 7410(m), 7509(b) (Clean Air Act Amendments of 1990, imposing sanctions on States if they fail to create approved State implementation plans); 20 U.S.C. § 6311 (No Child Left Behind Act, giving States the choice to opt out of the Act but imposing substantial requirements if they chose to accept federal funds); 42 U.S.C. § 1396 *et seq.* (Social Security Act of 1965, Title XIX, establishing Medicaid as a cooperative federal-state partnership); *see also Dole*, 483 U.S. 203; *Steward Machine Co. v. Davis*, 301 U.S. 548 (1937) (upholding federal tax on employers that was abated if the employers paid into a State unemployment plan that met federal specifications).

The premium assistance tax credit is no different. They are part of a classic Spending Clause program in which Congress used its power of the purse to induce States to establish State Exchanges so the federal government would not have to do so. This general theme recurs throughout the ACA: again and again, Congress created various incentives to induce employers, individuals, and States to take the actions Congress wanted them to take but could not or would not mandate. *See, e.g.*, *Nat'l Fed'n of Indep. Businesses v. Sebelius*, 132 S. Ct. 2566, 2593 (2012) ("*NFIB*") (opinion of Roberts, C.J.); *id.* at 2600 (majority opinion); *id.* at 2601-07 (opinion of Roberts, C.J., Breyer, Kagan, JJ.); *id.* at 2648, 2666-67 (Scalia, Kennedy, Thomas, Alito, JJ., dissenting) (considering the individual mandate and Medicaid expansion incentives).

For example, the ACA requires large employers to offer qualified health plans to full-time employees or be subject to an "assessable payment." 26 U.S.C. § 4980H. As construed by the Supreme Court, the Act requires individuals to maintain minimum essential health insurance coverage or pay a "tax," *NFIB*, 132 S. Ct. at 2600 (majority opinion) (construing 26 U.S.C. § 5000A), and requires States to expand Medicaid or face losing all federal Medicaid funding, *id.* at 2604 (opinion of Roberts, C.J., Breyer, Kagan, JJ.) (citing 42 U.S.C. § 1396c).[2] Indeed, Congress went to such extreme lengths to induce States to expand Medicaid, that Congress exceeded its power under the Taxing and Spending Clause, U.S. Const. art. I, § 8, cl. 1. *NFIB*, 132 S. Ct. at 2601-07 (opinion of Roberts, C.J., Breyer, Kagan, JJ.); *id.* at 2666-67 (Scalia, Kennedy, Thomas, Alito, JJ., dissenting).

Specifically with respect to encouraging States to establish their own Exchanges, the Act imposes a "maintenance-of-effort" requirement that prohibits States from tightening Medicaid eligibility standards until "an Exchange established by the State under section 18031 of this title is fully operational." 42 U.S.C. § 1396a(gg). It also provides start-up grants to States to defray the cost of establishing an Exchange. *Id.* § 18031(a). Conspicuously absent from the Act is

[2] In *NFIB*, the U.S. Supreme Court upheld the individual mandate as a tax, not a penalty, and invalidated portions of the Medicaid funding conditions. 132 S. Ct. at 2601, 2604-07. But this does not change the clear pattern in the ACA of Congress using financial incentives to encourage certain behaviors and discourage others. The premium assistance tax credit, which Congress used to induce States to establish State Exchanges, fits comfortably in this pattern.

any authorization of funding for HHS to create Federal Exchanges. *See id.* § 18041. Each of these examples shows that Congress knew what it was doing: Congress did not want to bear the burden of implementing certain parts of the ACA, but it could not directly require States to implement and enforce federal policies, so it relied on various inducements and encouragements to entice States to undertake the logistically and politically difficult task of implementing the ACA—even to the point of violating the limits on its authority to do so, *see NFIB*, 132 S. Ct. at 2601-07 (opinion of Roberts, C.J., Breyer, Kagan, JJ.); *id.* at 2666-67 (Scalia, Kennedy, Thomas, Alito, JJ., dissenting).

This pattern reinforces the plain language of the premium assistance tax credit, which Congress intended as an incentive for States to establish state-run Exchanges. It also exposes the absurdity of construing the Act to provide the subsidy through both State and Federal Exchanges—this would completely eliminate the incentive for States to set up their own Exchanges. Moreover, there were obvious political, practical, and financial advantages to persuading States to share the load of establishing and operating the Exchanges, including shared political accountability, technical and local expertise, and State funding for continued operation and maintenance of State Exchanges.

Congress purposely did not extend the premium assistance tax credit to Federal Exchanges because it would make no sense to do so in light of its goal to

induce States to establish Exchanges. Instead, Congress provided start-up grants to States for establishing Exchanges, 42 U.S.C. § 18031(a), offered subsidies to individuals in States that established one, 26 U.S.C. § 36B(a), (b), and restricted States' control over related programs until they did so, 42 U.S.C. § 1396a(gg). This system of incentives for States to participate, complemented by disincentives for non-participation, reflects Congress' aim and assumption that most if not all of the States would create their own ACA Exchanges. *See* Jonathan H. Adler & Michael F. Cannon, *Taxation Without Representation: The Illegal IRS Rule To Expand Tax Credits Under the PPACA*, 23 HEALTH MATRIX 119, 165-67 (2013).

This carefully chosen set of mutually reinforcing incentives gave States a choice: either set up a State Exchange and receive the benefits of federal subsidies and other inducements, or face the threat of fallback Federal Exchanges and forfeiting the perks of having "an Exchange *established by the State under [42 U.S.C. § 18031]*," 26 U.S.C. § 36B(c)(2)(A)(i). Thus it is fitting that the U.S. Supreme Court has "repeatedly characterized . . . Spending Clause legislation," such as the Exchange provisions of the ACA, "as much in the nature of a contract." *NFIB*, 132 S. Ct. at 2601 (opinion of Roberts, C.J., Breyer, Kagan, JJ.) (quoting *Barnes v. Gorman*, 536 U.S. 181, 186 (2002)) (internal quotation marks omitted); *see also id.* at 2659-60 (opinion of Scalia, Kennedy, Thomas, Alito, JJ., dissenting) (quoting same). The "legitimacy of Congress's exercise of the spending power . . .

rests on whether the State voluntarily and knowingly accepts the terms of the 'contract.'" *Id.* (opinion of Roberts, C.J., Breyer, Kagan, JJ.) (quoting *Pennhurst State Sch. & Hosp. v. Halderman*, 451 U.S. 1, 17 (1981)) (internal quotation marks omitted); *see also id.* at 2660 (opinion of Scalia, Kennedy, Thomas, Alito, JJ., dissenting) (same). It is "critical" that courts and Congress respect this limitation because it "ensur[es] that Spending Clause legislation does not undermine the status of the States as independent sovereigns in our federal system." *Id.* (opinion of Roberts, C.J., Breyer, Kagan, JJ.); *see also id.* at 2659-60 (opinion of Scalia, Kennedy, Thomas, Alito, JJ., dissenting).

Here, the plain text of the ACA manifests Congress' clear intent to induce States to establish State Exchanges. It deliberately limited the premium assistance tax credit to State Exchanges to achieve this goal. Now the IRS seeks to change the plain terms of the "contract" Congress offered the States. This not only exceeds the IRS' authority and is contrary to law, but it "undermine[s] the status of the States as independent sovereigns in our federal system," *id.* (opinion of Roberts, C.J., Breyer, Kagan, JJ.); *see also id.* at 2659-60 (opinion of Scalia, Kennedy, Thomas, Alito, JJ., dissenting). The federal government should be held to the deal Congress struck. No general purpose to "ensure broad access to affordable health coverage for all," JA 311, or absence of "direct support in the legislative history of the ACA," JA311, can overcome the unequivocal text of the Act and the purpose of

the premium assistance tax credit to entice States to establish Exchanges. *See Nahigian v. Juno-Loudoun, LLC*, 677 F.3d 579, 588 (4th Cir. 2012) (because section 36B and the Exchange provisions are clear on their face, the IRS "cannot rewrite them to fit its own conception of how [the ACA] should work").

III. Allowing The IRS To Repurpose The Premium Assistance Tax Credit—Contrary To The Act's Plain Text And The Unequivocal Purpose Of The Credit—Deprives States Of A Choice Congress Gave Them.

Notwithstanding Congress' carefully calibrated incentives for States to establish their own Exchanges, 34 States—including *Amici* States—declined to take the bait. Allowing a federal agency to eliminate the statutory distinction and override *Amici* States' decisions by extending the premium assistance tax credit to them and their citizens anyway will have profoundly negative consequences in those States: the availability of the premium assistance tax credit on Federal Exchanges effectively extends the individual mandate to many individuals who would otherwise be exempt and triggers the employer mandate. Exercising their option under the ACA to avoid these consequences, *Amici* States rejected Congress' inducements and chose not to establish State Exchanges. The IRS Rule unlawfully denies States the benefits of their decision, while simultaneously imposing on them many of the burdens of having a State Exchange, burdens the States consciously chose to avoid.

The consequences of the unlawful IRS Rule stem from the interconnectedness of different aspects of the intricate regulatory scheme Congress created. Most directly, the availability of the premium assistance tax credit extends the individual mandate to many individuals who otherwise would be exempt. The individual mandate requires all "applicable individual[s]" to obtain "minimum essential coverage." 26 U.S.C. § 5000A(a). The Act imposes a "penalty" on any "applicable individual" who "fails to meet [this] requirement." *Id.* § 5000A(b)(1). But "[i]ndividuals who cannot afford coverage," are exempt from the "penalty." *Id.* § 5000A(e)(1). This unaffordability exemption applies only if the cost of health insurance exceeds eight percent of an "individual's household income for the taxable year." *Id.* § 5000A(e)(1)(A). For "an individual eligible only to purchase minimum essential coverage" in the individual market within a State, the cost of health insurance is calculated as the cost of the cheapest plan on an Exchange "reduced by the amount of the credit allowable under section 36B," *id.* § 5000A(e)(1)(B)(ii), *i.e.*, minus the premium assistance tax credit available for plans purchased on a State Exchange, 26 U.S.C. § 36B(c)(2)(A)(i).

The IRS Rule therefore expands the number of individuals subject to the mandate by making the premium assistance tax credit "allowable" in the States with Federal Exchanges. Absent the IRS Rule, these individuals would be free to buy cheaper, high-deductible plans, *see* 42 U.S.C. § 18022(e)(1)(A), (2), or forgo

health insurance altogether without being subject to penalties. Appellants in this case provide the perfect example of this. The District Court correctly found that Appellants have standing because "their economic injury is real and traceable to the IRS Rule," which Appellants say would "den[y] them an exemption from the Minimum Coverage Provision and, thus, the option not to buy any health insurance at all." JA298. As a consequence, individuals like Appellants are forced either to "buy insurance or pay the Minimum coverage Provision penalty," JA298-JA299—even though Congress exempted them from the mandate.

Congress gave States the option to avoid this consequence for some of their citizens by permitting States to elect not to establish State Exchanges. *Amici* States exercised this option. The IRS should not be allowed to rewrite the statute to deny States' and their citizens the benefit of their congressionally-authorized decisions not to establish State Exchanges.

The IRS Rule also unlawfully triggers the employer mandate in States, like *amici*, that declined to set up State Exchanges. The ACA imposes an "assessable payment" on any employer with 50 or more employees that does not "offer to its full-time employees . . . the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan." 26 U.S.C. § 4980H(a). A "full-time employee" is one who works 30 or more hours in a week. *Id.* § 4980H(c)(4). But the "assessable payment" applies only if "at least one full-time employee" enrolls

in a health insurance "plan with respect to which an applicable premium tax credit . . . is allowed or paid with respect to the employee." *Id.* § 4980H(a)(2). So under the plain text of the ACA—which does not make available the premium assistance tax credit through Federal Exchanges—the employer mandate and related penalties would not apply to large employers in *Amici* States, much less the States themselves. Yet the IRS Rule subjects large employers in *Amici* States (including the States as employers) to the employer mandate and the threat of an "assessable payment" if the employers do not comply.

Exercising the option granted by the ACA—and required by the Constitution—*Amici* States chose not to establish their own Exchanges. This decision should have entitled them to avoid extending the individual mandate to otherwise-exempt individuals and avoid the employer mandate altogether. As the Act itself acknowledges, it is the States' sovereign prerogative to implement state policy that spares low-income individuals from the individual mandate and employers from the employer mandate. *See* 42 U.S.C. § 18041(b), (c); *see also Printz*, 521 U.S. at 925, 933, 935. Despite the ACA's various inducements and restrictions designed to elicit State cooperation, *Amici* States have chosen "to defend their prerogatives by adopting 'the simple expedient of not yielding' to federal blandishments" because "they do not want to embrace the federal policies as their own." *NFIB*, 132 S. Ct. at 2603 (opinion of Roberts, C.J., Breyer, Kagan,

JJ.) (quoting *Massachusetts v. Mellon*, 262 U.S. 447, 482 (1923)). *Amici* States have made policy determinations about the regulatory environment they want to provide for individual residents and employers. Many of them have passed laws effectuating their decision not to establish Exchanges. *See* National Conference of State Legislatures, *State Legislation and Actions Opting-out or Opposing Certain Health Reforms*, http://www.ncsl.org/documents/summit/summit2013/online-resources/State-Legislation-Opt-out.pdf. The IRS Rule interferes with these decisions, and largely obliterates the discretion Congress reserved to the States under the ACA, as well as the States' sovereignty under the Constitution.

By rewriting the Act, the IRS has imposed a substantial economic burden on States that chose not to establish State Exchanges. A Congressional Budget Office ("CBO") report just released on February 4, 2014, quantifies this very real burden. CBO, *The Budget and Economic Outlook: 2014 to 2024*, *available at* http://www.cbo.gov/sites/default/files/cbofiles/attachments/45010-Outlook2014.pdf, Appx. C, at 117-24 (last visited Feb. 4, 2014). It finds that the premium assistance tax credit will decrease the labor supply, *id.* at 120, and the employer mandate will increase labor costs and unemployment, *id.* at 124. Overall, the report estimates that the ACA will reduce full-time equivalent employment by "about 2.0 million in 2017, rising to about 2.5 million in 2024, compared with what would have occurred in the absence of the ACA." *Id.* at 127. The IRS Rule would deprive

States of the economic benefit of their decision not to establish State Exchanges. Notwithstanding the IRS' unlawful efforts to amend the statute by regulatory fiat, the plain language of the ACA authorizes States to choose not to establish State Exchanges. The Court should reject the IRS' attempt to saddle nonconsenting States, like *amici*, with the substantial economic burdens of a flawed policy that the States properly and deliberately opted out of.

IV. Congress Cannot Co-opt States' Sovereign Prerogatives By Unilaterally Nominating The Federal Government—*Sub Silentio*—To Act On Behalf Of States In Order To Contradict States' Reasoned And Deliberate Policy Decisions.

The IRS contends that the phrase "established by the *State* under *[42 U.S.C. § 18031]*," 26 U.S.C. § 36B(c)(2)(A)(i), actually includes Exchanges "established by the *federal government* (HHS) under *42 U.S.C. § 18041*." But in Section 36B itself, Congress twice stated that it intended the premium assistance tax credit to be available only on State Exchanges, that is, Exchanges "established by the State." 26 U.S.C. § 36B(c)(2)(A)(i). The Act defines "State" as "each of the 50 States and the District of Columbia." 42 U.S.C. § 18024(d). And if this were not clear enough, it cited the section of the Act that directs States to establish Exchanges—Section 18031. 26 U.S.C. § 36B(c)(2)(A)(i). "State" means "State," and the federal government is not a "State."

The fiction the IRS has promoted—that the federal government can create "an Exchange established by the State under [42 U.S.C. § 18031]" on behalf of a

State by standing in the shoes of the State—is preposterous. Congress went out of its way to provide for two types of Exchanges in two separate provisions of the Act: Section 18031 provides for State Exchanges; Section 18041 provides for Federal Exchanges. The Act directs the federal government to establish an Exchange only if a State declines to do so. 42 U.S.C. § 18041(b), (c). And it must "establish and operate such Exchange *within* the State," *id.* § 18041(c)—not "*for*" the State or "*on behalf of*" the State as the IRS contends.

The premium assistance tax credit provision at issue here acknowledges that there could be Exchanges "within a State" but not "established by the State." *See* 26 U.S.C. § 36B(b)(2)(A); *see also id.* § 36B(f)(3). Thus the two types of Exchanges are not interchangeable. *See* Adler & Cannon, *supra*, at 158-64.

The IRS' view of the ACA's Exchange provisions makes even less sense in light of the constitutional principles that animated the Act's cooperative federalism structure in the first place. The reason Congress created fallback Federal Exchanges was because the Tenth Amendment prohibits Congress from outright requiring States to implement and enforce federal regulations. *Printz*, 521 U.S. at 935. Yet allowing the federal government to stand in the shoes of States—and create "an Exchange established by the State under [42 U.S.C. § 18031]" on behalf of that State—only after the State has declined to establish the State Exchange itself, 42 U.S.C. § 18041(b), (c), cannot be squared with our system of federalism.

Could Congress authorize the IRS to pass state laws on behalf of a State (*New York v. United States*, 505 U.S. 144 (1992)), or to hire additional state sheriffs to enforce federal law on behalf of a State (*Printz v. United States*, 521 U.S. 898 (1997))? Certainly not, but that is precisely the power the IRS is asserting and the District Court upheld in this case.

Because the fallback Federal Exchanges come into play only *after* a State has declined to establish a State Exchange, 42 U.S.C. § 18041(b), (c), it offends States' constitutionally-recognized sovereignty—and basic logic—to allow the federal government to act on behalf of the State for the exclusive purpose of repudiating the State's decision. Yet this is exactly what the District Court has allowed the IRS to do.

V. Because States Are "Large Employers" Under The ACA, The IRS Rule Violates The Tenth Amendment By Extending The Employer Mandate To *Amici* States.

The ACA treats States no differently than any other employer for purposes of imposing the employer mandate and its onerous "assessable payments." *See* 26 U.S.C. § 4980H(a), (c)(2). The only way for States to avoid the burdensome mandate is to opt out of establishing a State Exchange. *See id.* § 36B(b)(2)(A); *id.* § 4980H(a), (c)(2). And that is exactly what *Amici* States did. Yet the IRS seeks again to eliminate another of the options Congress gave the States by extending the mandate to States (like *amici*) that chose not to set up their own Exchange.

Forcing the employer mandate on States without their consent, as the IRS Rule does, dramatically interferes with state sovereignty and violates the Tenth Amendment. The Court should avoid even approaching these constitutional shoals by invalidating the IRS Rule as inconsistent with the plain text of the Act itself. But if the Court allows the IRS to extend the premium assistance subsidy to Federal Exchanges, which in turn would extend the employer mandate to *Amici* States and others that chose not to establish State Exchanges, the employer mandate would violate the Tenth Amendment as applied to such States in their capacity as employers.

A. The Court Should Invalidate the IRS Rule To Avoid The Serious Constitutional Issues The Rule Creates As A Result Of Extending The Employer Mandate To Nonconsenting States.

Because *Amici* States chose not to establish State Exchanges, under the plain terms of the ACA, they would be free to offer whatever health insurance they wanted to their employees—and free to offer no insurance at all. *See* 26 U.S.C. § 36B(b)(2)(A); 26 U.S.C. § 4980H(a), (c)(2). But the IRS Rule ignores *Amici* States' choice, requiring them to provide a federally mandated level of health insurance to employees who work 30 hours or more per week, and imposes the ACA's harsh "assessable payments" if States do not comply. *See* 26 C.F.R. § 1.36B-2(a)(1); 26 C.F.R. § 1.36B-1(k); 45 C.F.R. § 155.20; 77 Fed. Reg. 30,377-78, 30,387; *see also* 26 U.S.C. § 4980H(a), (c)(2).

As discussed in more detail below, allowing the IRS to extend the employer mandate to States that rejected the benefits and burdens of establishing a State Exchange—including the employer mandate—would dramatically interfere with state sovereignty. Just as the Supreme Court did in *Gregory v. Ashcroft*, this Court should avoid these serious constitutional issues by construing the statute not to apply to nonconsenting States. 501 U.S. 452, 464 (1991).

It is "incumbent upon the federal courts to be certain of Congress' intent before finding that federal law overrides . . . the usual constitutional balance of federal and state powers." *Gregory*, 501 U.S. at 460-61 (quoting *Atascadero State Hosp. v. Scanlon*, 473 U.S. 234, 242 (1985)) (internal quotation marks omitted). If Congress intends to alter this balance, it "must make its intention to do so 'unmistakably clear in the language of the statute.'" *Id.* at 460-61 (quoting *Atascadero*, 473 U.S. at 242). The employer mandate contains no such clear statement. And because Congress designed the employer mandate to hinge on a State choosing to establish an Exchange, it is apparent that Congress' intent was just the opposite: to preserve—not upset—the state-federal balance.

B. If The Court Approves The IRS Rule, Which Extends The Employer Mandate To *Amici* And Other Nonconsenting States, The Employer Mandate As Applied To Those States Would Violate The Tenth Amendment.

Our Constitution established a "system of dual sovereignty between the States and the Federal Government." *Gregory*, 501 U.S. at 457. Although "States

surrendered many of their powers to the new Federal Government, they retained 'a residuary and inviolable sovereignty.'" *Printz*, 521 at 918-19 (quoting The Federalist No. 39 (J. Madison)). As the Tenth Amendment provides, "[t]he powers not delegated to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people." U.S. Const. amend. X.

As "joint sovereigns" with the federal government, States "retain substantial sovereign authority under our constitutional system." *Gregory*, 501 U.S. at 457-58. While the federal government's powers are "few and defined," state government powers "extend to all the objects which, in the ordinary course of affairs, concern the lives, liberties, and properties of the people, and the internal order, improvement, and prosperity of the State." *Gregory*, 501 U.S. at 458 (quoting The Federalist No. 45 (J. Madison)) (internal quotation marks omitted).

The employer mandate, if applied via the IRS Rule to *Amici* States and others that chose not to establish a State Exchange, would interfere with essential attributes of state sovereignty. By requiring States to provide minimum essential health insurance coverage to all employees who work 30 or more hours in a week, the employer mandate would dramatically diminish States' sovereign discretion to define the terms of employment for those providing governmental services. The employer mandate would affect staffing decisions and diminish the States'

discretion regarding how best to deliver these services. The substantial financial burden the employer mandate may impose on States could deeply influence a host of state and local public policy decisions, especially given that many States continue to wrestle with budgetary constraints. Government programs concerning public safety and general welfare—which are core State prerogatives—would suffer. Our system of "dual sovereignty" simply does not permit this intrusion.

Garcia v. San Antonio Metropolitan Transit Authority, held that Congress, when legitimately exercising its commerce power, may subject States to generally applicable employer regulations even if the regulations interfere with essential attributes of state sovereignty. 469 U.S. 528, 556-57 (1985). *Garcia* reasoned that "affirmative limits on the Commerce Clause power" are not necessary to protect State sovereignty because the "political process ensures that laws that unduly burden the States will not be promulgated." *Id.* Yet here, the political process was manipulated. *See* Brief of *Amici Curiae* U.S. Representatives Trent Franks, et al., *Sissel v. U.S. Dept. of Health & Human Servs.*, No. 13-5202 (D.C. Cir. Dec. 3, 2013) (arguing that enactment of the ACA violated the Origination Clause). *Garcia* itself recognized that, to avoid certain unnamed "'horrible possibilities,'" "the constitutional structure might impose [affirmative limits] on federal action affecting the States under the Commerce Clause." 469 U.S. at 556 (quoting *New York v. United States*, 326 U.S. 572, 583 (1946) (opinion of Frankfurter, J.)); *see*

South Carolina v. Baker, 485 U.S. 505, 513 (1988) (noting *Garcia* "left open the possibility that some extraordinary defects in the national political process might render congressional regulation of state activities invalid under the Tenth Amendment"). If the Tenth Amendment's role as a substantive federalism safeguard ever applies, then surely it would apply here.

In any event, on the Supreme Court's "unsteady path" of Tenth Amendment jurisprudence, *New York*, 505 U.S. at 160, *Garcia* has been overtaken by more recent Supreme Court precedents. For example, after the Court rejected court-enforceable substantive limits on Congress' Commerce Clause power in *Garcia*, it has on numerous occasions identified and enforced real limits on Congress' ability to interfere with state sovereignty. *See, e.g.*, *New York*, 505 U.S. at 177 (striking down federal law as unconstitutional incursion on state sovereignty); *Printz*, 521 U.S. at 935 (same); *see also Bd. of Trs. of Univ. of Ala. v. Garrett*, 531 U.S. 356, 374 (2001) (rejecting effort to treat States like other employers under the Americans with Disabilities Act); *United States v. Morrison*, 529 U.S. 598, 627 (2000) (striking down federal law as exceeding federal commerce power and intruding on state sovereignty); *United States v. Lopez*, 514 U.S. 549, 567 (1995) (same).

The Supreme Court's approach to protecting States' sovereign authority over the almost three decades since *Garcia* was decided casts serious doubt on the

continuing vitality and scope of *Garcia*. That is particularly true in a case such as this, when even *Garcia* acknowledged that a substantive Tenth Amendment safeguard applies where defects in the political process render the Tenth Amendment a practical nullity.[3]

C. If The Employer Mandate—Like The Individual Mandate—Is A Tax, It Violates The States' Right To Intergovernmental Tax Immunity.

In *NFIB v. Sebelius*, the Supreme Court upheld the ACA's individual mandate as a tax, and further held that the mandate was not a proper exercise of Congress' commerce power. *See* 132 S. Ct. at 2594-2601 (majority opinion). The "assessable payment" for violating the employer mandate seems indistinguishable, and if treated as a tax, that statutory requirement would violate the intergovernmental tax immunity doctrine as applied to States. 26 U.S.C. § 4980H(a), (b), (c)(2)(A), (c)(4)(A).[4]

The Supreme Court long has recognized that the "United States lacks the authority to tax the property or revenues of States or municipalities, since their independence from federal control is secured by the Tenth Amendment." *South*

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[3] In light of the Supreme Court's post-*Garcia* decisions, cited above, even reaching the question of whether *Garcia* forecloses *Amici* States' Tenth Amendment argument raises serious constitutional questions that the Court should avoid by simply invalidating the IRS regulations. *See supra* Part V.A.

[4] *NFIB* upheld the individual mandate as a "tax" under the Taxing Clause of Article I, § 8, cl. 1, but held it was not a "tax" for purposes of the Anti-Injunction Act, 26 U.S.C. § 7421(a). 132 S. Ct. at 2584, 2600. *Amici* States' intergovernmental tax immunity argument only relates to the former, not the latter.

Carolina v. Regan, 465 U.S. 367, 405 (1984) (citing *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429 (1895)); *Metcalf & Eddy v. Mitchell*, 269 U.S. 514, 522 (1926) ("[A]gencies through which either government[—State or federal—] immediately and directly exercises its sovereign powers, are immune from the taxing power of the other."). Yet the "assessable payment" would do exactly that.

CONCLUSION

"The States are separate and independent sovereigns. Sometimes they have to act like it." *NFIB*, 132 S. Ct. at 2603 (opinion of Roberts, C.J., Breyer, Kagan, JJ.). That is exactly what *Amici* States have tried to do here. Congress gave the States a choice regarding the health insurance Exchanges, and two-thirds of the States made a deliberate and reasoned decision not to create such Exchanges themselves. To protect *Amici* States' decisions to opt out of the benefits and burdens of establishing a State Exchange under the ACA, and to preserve their position as "joint sovereigns" in our federalist system, *Amici* States respectfully ask the Court to reverse the District Court's decision and invalidate the unlawful IRS Rule that contravenes the Act's plain language and that purports to rewrite the deal Congress struck with the States.

Dated: March 10, 2014

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3. This brief has been scanned for viruses using Sophos Endpoint Security and Control (version 10.3), and no viruses were detected.
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DATED: March 10, 2014 /s/ Jeffrey A. Chanay

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Pursuant to Federal Rule of Appellate Procedure 25(d), I hereby certify that on March 10, 2014, the foregoing Brief Of *Amici* States In Support of Reversal was electronically filed with the Clerk of Court for the United States Court of Appeals for the Fourth Circuit using the CM/ECF system. I certify that the participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system. I also certify that I caused eight paper copies to be delivered by Federal Express to the Clerk's Office.

DATED: March 10, 2014 /s/ Jeffrey A. Chanay

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