[EN BANC ORAL ARGUMENT SCHEDULED FOR DECEMBER 17, 2014]

No. 14-5018

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

JACQUELINE HALBIG, et al.,

Appellants,

v.

SYLVIA MATHEWS BURWELL, SECRETARY OF HEALTH AND HUMAN SERVICES, et al.,

Appellees.

On Appeal from the United States District Court for the District of Columbia (No. 13-623 (PLF))

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

DEREK SCHMIDT
Kansas Attorney General
Jeffrey A. Chanay
Chief Deputy Attorney General
Counsel of Record
Stephen R. McAllister
Solicitor General
Dwight R. Carswell
Assistant Attorney General
Memorial Building
120 SW 10th, 2nd Floor
Topeka, Kansas 66612
(785) 296-2215

Counsel for Amici Curiae

[Additional Counsel Listed On Inside Cover]

ADDITIONAL COUNSEL

JON BRUNING, Attorney General of the State of Nebraska

CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

Amici States certify as follows:

A. Parties And Amici

All parties, intervenors, and amici appearing before the district court and in this court will be listed in the Brief for Appellants. In addition, the now-vacated Opinion of the Court, 758 F. 3d 390 (D.C. Cir. 2014), contains a listing of all parties, intervenors, and amici that have appeared in the district court and in this court.

B. Rulings Under Review

References to the rulings at issue will appear in the Brief for Appellants.

C. Related Cases

On July 22, 2014, a panel of this Court issued an opinion reversing the District Court and remanding the case with instructions to vacate the IRS Rule. *Halbig v. Burwell*, 758 F.3d 390 (D.C. Cir. 2014). The en banc Court vacated that judgment in the order granting rehearing en banc. No. 14-5018, Document No. 1510560, Order of the En Banc Court (September 4, 2014).

TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

GLOSSARY viii

STATUTES AND REGULATIONS ix

IDENTITY AND INTEREST OF *AMICI CURIAE* 1

SUMMARY OF ARGUMENT 2

ARGUMENT 6

I. The IRS Rule Extends Premium Assistance Tax Credits To Federal Exchanges In Direct Violation Of The Unambiguous Text Of The ACA 6

II. The IRS Rule Not Only Violates The Text Of The ACA, It Contradicts The Structure Of The Act And The Purpose Of Limiting The Premium Assistance Tax Credits To State Exchanges. 8

III. Allowing The IRS To Repurpose The Premium Assistance Tax Credits—Contrary To The Plain Text Of The Act And Unequivocal Purpose Of The Credits—Deprives States Of A Choice Congress Gave Them 14

IV. Congress Cannot Co-opt States' Sovereign Prerogatives By Unilaterally Nominating Itself—*Sub Silentio*—To Act On Behalf Of States In Order To Contradict States' Reasoned Policy Judgments. 18

V. Because States Are "Large Employers" Under The ACA, The IRS Rule Violates The Tenth Amendment By Extending The Employer Mandate To *Amici* States. 21

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. 23

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. 24

C. If The Employer Mandate—Like The Individual Mandate—Is A Tax, It Violates States' Right To Intergovernmental Tax Immunity 28

CONCLUSION 29

CERTIFICATE OF COMPLIANCE 31

CERTIFICATE OF SERVICE 32

TABLE OF AUTHORITIES

Page(s)

CASES

Atascadero State Hosp. v. Scanlon,
473 U.S. 234 (1985) 24

Barnes v. Gorman,
536 U.S. 181 (2002) 12

Bd. of Trs. of Univ. of Ala. v. Garrett,
531 U.S. 356 (2001) 27

Cal. State Bd. of Optometry v. Fed. Trade Comm'n,
910 F.2d 976 (D.C. Cir. 1990) 23, 24

Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.,
467 U.S. 837 (1984) 7

Garcia v. San Antonio Metro. Transit Auth.,
469 U.S. 528 (1985) 24, 26, 27

**Gregory v. Ashcroft*,
501 U.S. 452 (1991) 23, 24, 25

Massachusetts v. Mellon,
262 U.S. 447 (1923) 17

Metcalf & Eddy v. Mitchell,
269 U.S. 514 (1926) 29

---

* Authorities upon which we chiefly rely are marked with asterisks.

*_Nat'l Fed'n of Indep. Businesses v. Sebelius_,
132 S. Ct. 2566 (2012).. 9, 10, 11, 12, 13, 17, 28, 29

*_New York v. United States_,
505 U.S. 144 (1992)... 8, 21, 27

Oklahoma v. Burwell,
No. 11-CV-30, slip op. at 5–8 (E.D. Okla. Sept. 30, 2014)……………………22

Pennhurst State Sch. & Hosp. v. Halderman,
451 U.S. 1 (1981)..13

Pollock v. Farmers' Loan & Trust Co.,
157 U.S. 429 (1895)..29

*_Printz v. United States_,
521 U.S. 898 (1997).. 6, 17, 20, 21, 24, 27

South Carolina v. Baker,
485 U.S. 505 (1988)..26

South Carolina v. Regan,
465 U.S. 367 (1984)..28

South Dakota v. Dole,
483 U.S. 203 (1987)..8, 9

Steward Machine Co. v. Davis,
301 U.S. 548 (1937)..9

United States v. Lopez,
514 U.S. 549 (1995)..27

United States v. Morrison,
529 U.S. 598 (2000)....................27

CONSTITUTIONAL PROVISIONS

U.S. Const. amend. X....................25

U.S. Const. art. I, § 8, cl. 1....................10

STATUTES

20 U.S.C. § 6311....................8

*26 U.S.C. § 36B....................4, 7, 11, 12, 13, 15, 19, 20, 21, 22, 23

*26 U.S.C. § 4980H....................9, 16, 22, 23, 28

26 U.S.C. § 5000A....................10, 14, 15

42 U.S.C. § 1396....................9

42 U.S.C. § 1396a....................10, 12

42 U.S.C. § 1396c....................10

42 U.S.C. § 18022....................15

42 U.S.C. § 18024....................19

*42 U.S.C. § 18031....................6, 7, 10, 11, 12, 13, 15

*42 U.S.C. § 18041....................6, 7, 10, 17, 20, 21, 22

42 U.S.C. § 7410....................8

42 U.S.C. § 7509 8

5 U.S.C. § 706 7

REGULATIONS

*26 C.F.R. § 1.36B-1 ....7, 23

*26 C.F.R. § 1.36B-2 ....7, 23

45 C.F.R. § 155.20 ....7, 23

OTHER AUTHORITIES

*77 Fed. Reg. 30,377 ....7, 23

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) 26

Congressional Budget Office, *The Budget and Economic Outlook: 2014 to 2024*, *available at* http://www.cbo.gov/sites/default/files/cbofiles/attachments/45010-Outlook2014_Feb.pdf 18

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) 12, 20

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 17

The Federalist No. 39 (J. Madison) 24

The Federalist No. 45 (J. Madison) 25

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

STATUTES AND REGULATIONS

All pertinent statutes and regulations are contained in the Statutory & Regulatory Addendum to Brief for Appellants.

IDENTITY AND INTEREST OF *AMICI CURIAE*

Amici States seek to protect their decision to opt out of the benefits and burdens associated with establishing state-run marketplaces for selling qualified health insurance plans under the Patient Protection and Affordable Care Act ("ACA" or "the Act").[1] The Act expressly gives States this option. In States that opt out, federally funded premium assistance tax credits are 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' policy choice by extending federal premium assistance subsidies to them anyway. As a result, the regulations expose otherwise-exempt individuals to the individual mandate and trigger the employer mandate in States—including *amici*—that properly chose to avoid these additional regulatory burdens.

The IRS regulations (together, "the IRS Rule" or "the Rule") undo the cooperative federalism structure of the Exchange provisions of the ACA 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

---

[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." D.C. Cir. Rule 29(d) and the Court's order do not require government *amici* to join in a single brief with other *amici* on the same side.

sovereign authority to pursue the economic and social policies they choose to promote the welfare of their citizens.

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. The States of Kansas and Nebraska also file this brief to support the interests of Plaintiff-Appellant Community National Bank, which is situated near the Kansas-Nebraska border.

SUMMARY OF ARGUMENT

Notwithstanding its overall labyrinthine complexity, the ACA is surprisingly clear on the critical point at issue in this case: federal subsidies for health insurance are 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 subsidies are 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 refundable tax credits to subsidize premiums for low- and middle-income Americans who purchase health insurance through a state-run Exchange. The subsidies, however, had collateral consequences for States: they would extend the individual mandate to individuals who otherwise would be exempt, and would trigger the employer mandate, which requires all large employers in the State (including the States) 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 premium assistance subsidies. Indeed, the Act would not make sense if the subsidies were available on federal

Exchanges because that would remove the incentive Congress created to encourage States to create their own Exchanges.

The Act is explicit and inescapable: federal subsidies for health insurance are 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 premium assistance tax credits 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.

To get around the plain text of the Act, the District Court found that Congress intended to allow the federal government to act as a State for purposes of setting up an Exchange under the ACA, apparently believing that the Court had the power to dispense with Congress' enacted bait for the States and instead simply use a net to capture all of the States. This confounding interpretation of the Act bears no relation to the actual text of the Act and ignores States' separate sovereignty. Replacing Congress' unequivocal intent with the IRS's own policy preferences, the IRS rewrote 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 extended 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. What's more, 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 IRS Rule is at odds with the plain language of the premium assistance tax credit provision. But instead of taking Congress at its word and confining the IRS to its statutory authority, the District Court did just the opposite, turning to one-sided policy rationales, the absence of legislative history, "anomalies" in the operation of other provisions of the ACA, and a troubling theory that the U.S. Department of Health and Human Services ("HHS") "stands in the shoes" of a State when it creates federal Exchanges in a vain attempt to justify its shocking result.

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 federal subsidies to State Exchanges; (3) undermines States' policy 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 panel correctly concluded that the District Court's legally insupportable decision should be reversed.

ARGUMENT

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

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 simply compelling the States to establish Exchanges would violate the Tenth Amendment, *see Printz v. United States*, 521 U.S. 898, 935 (1997); *New York v. United States*, 505 U.S. 144 (1992), Congress gave States the choice to opt out. In States that elected not to establish an Exchange, Congress created fallback federal Exchanges by requiring 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 42 U.S.C. § 18031, or accept the fallback federal exchange under 42 U.S.C. § 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 premium assistance tax credits 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: premium assistance tax credits are exclusively available on Exchanges "established by the State under [Section 18031]," *id.*; the subsidies are *not* available on Exchanges established by the federal government under Section 18041. Yet this is exactly what the IRS Rule does; it extends premium assistance tax credits 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 "[o]n its face, the plain language" of the premium assistance tax credits provision "appears to" foreclose the IRS Rule. *Halbig v. Sebelius*, No. 13-623, 2014 WL 129023, at *13 (D.D.C. Jan. 15, 2014). 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* 5 U.S.C. § 706(2). As the panel recognized, the Supreme Court

repeatedly has held that "an agency may not rewrite clear statutory terms to suit its own sense of how the statute should operate." Panel Op. at 40 (quoting *Util. Air Regulatory Group v. EPA*, 134 S. Ct. 2427, 2446 (2014)).

II. The IRS Rule Not Only Violates The Text Of The ACA, It Contradicts The Structure Of The Act And The Purpose Of Limiting The Premium Assistance Tax Credits To State Exchanges.

Instead of ending the matter and invalidating the unlawful IRS Rule, however, the District Court turned to one-sided policy rationales and "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 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 subsidies 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).

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).

The premium assistance tax credits are 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) (altogether holding that the individual mandate exceeds Congress' commerce power, but not its taxing and spending power, and that the Medicaid expansion exceeded Congress' taxing and spending power).

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). And tellingly, the Act does not

---

[2] In *NFIB*, the U.S. Supreme Court interpreted the individual mandate to be 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.

authorize any funding for HHS to create federal Exchanges. *See id.* § 18041. Each of these examples shows that Congress knew what it was doing: it 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 tried to use various inducements and encouragements to impel 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 subsidies for both State and federal Exchanges—this would completely eliminate the incentives for States to set up their own Exchanges. Moreover, there were obvious political, practical, and financial advantages to persuading the 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 credits to federal exchanges because it would make no sense to do so in light of its goal to

induce States to establish Exchanges. It provided start-up grants to States to establish 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, "Spending Clause legislation," such as the Exchange provisions of the ACA, is "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 thus 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' intent to induce States to establish State Exchanges. The Act deliberately limited premium assistance tax credits 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 "provide affordable health care to virtually all Americans," 2014 WL 129023, at *16, can overcome the unequivocal text of the Act and purpose of the premium assistance tax credits in enticing States to establish Exchanges.

III. Allowing The IRS To Repurpose The Premium Assistance Tax Credits—Contrary To The Plain Text Of The Act And Unequivocal Purpose Of The Credits—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. Overriding *Amici* States' decisions by extending premium assistance tax credits to them and their citizens anyway will have profoundly negative consequences in those States: the availability of premium assistance tax credits 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 benefit of their decision, while sticking them with many of the burdens.

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 premium assistance tax credits 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 credits 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 credits "allowable" in the States with federal Exchanges. Under the Act as written, 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. As a consequence of the IRS Rule, however, these individuals are forced either to buy health insurance or pay a "penalty"—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 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 provide tax credits through federal Exchanges—the employer mandate and related penalties would not apply to large employers in *Amici* States. Yet the IRS Rule subjects large employers to the employer mandate and the threat of an "assessable payment" if they 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); *Printz*, 521 U.S. at 925, 933, 935.

Here, the *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, undermining the discretion reserved to the States under the ACA and the Constitution.

The unlawful IRS Rule also imposes a substantial economic burden on States that chose not to establish State Exchanges. A Congressional Budget Office ("CBO") report 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_Feb.pdf, Appx. C, at 117-24 (last visited Sept. 24, 2014). The report finds that the premium assistance tax credits 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.

Thus, 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 Itself—*Sub Silentio*—To Act On Behalf Of States In Order To Contradict States' Reasoned Policy Judgments.

The District Court acknowledged that "[o]n its face, the plain language" of the premium assistance tax credits provision "appears to" limit the subsidy to State Exchanges. 2014 WL 129023, at *13. It also noted that interpreting the phrase,

"'established *by the State* under [42 U.S.C. § 18031],'" to limit the subsidy to state-established Exchanges "seem[s] . . . more intuitive" than the federal government's argument that the phrase "refer[s] to Exchanges created by a state *or* by HHS." *Id.* at *14 (quoting 26 U.S.C. § 36B(b)-(c)). The District Court's equivocal understatements are astonishing in light of the unambiguous statute at issue here.

Risking redundancy, the federal government's argument is so counterintuitive and atextual that it bears repeating: 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*." In Section 36B itself, Congress twice stated that it intended premium assistance tax credits 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."

Yet the District Court held that "even where a state does not actually establish an Exchange, the federal government can create 'an Exchange established

by the State under [42 U.S.C. § 18031]' *on behalf of* that state." 2014 WL 129023, at *14. As a matter of statutory interpretation, it is hard to make sense of this reading of the statute. 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 District Court concluded.

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 District Court's decision makes even less sense in light of the federalism 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 it from outright requiring States to implement and enforce federal regulations. *Printz*, 521 U.S. at 935. Yet the District Court construed the statute to allow 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," 2014 WL 129023, at *14—once the State declined to establish the State Exchange itself. 42 U.S.C. § 18041(b), (c).

But 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 in to play only *after* a State has declined to establish a State Exchange, 42 U.S.C. § 18041(b), (c), it offends States' separate 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. The District Court's decision should be reversed.

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). In a recent decision invalidating the IRS Rule as inconsistent with the plain language of the ACA, a federal district court held that the State of Oklahoma had standing to challenge the IRS Rule for precisely this

reason. *See State of Oklahoma v. Burwell*, No. 11-CV-30, slip op. at 5–8 (E.D. Okla. Sept. 30, 2014). 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 to eliminate the very option 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 premium assistance subsidies 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 impose 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 U.S. 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); *see also Cal. State Bd. of Optometry v. Fed. Trade Comm'n*, 910 F.2d 976, 981-92 (D.C. Cir. 1990).

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). This "rule of statutory construction serves to ensure that the States' sovereignty interests are adequately protected by the political process." *Cal. State Bd. of Optometry*, 910 F.2d at 981 (citing *Garcia v. San Antonio Metro. Transit Auth.*, 469 U.S. 528, 547-55 (1985)). The employer mandate contains no such clear statement. And because the employer mandate hinges 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 U.S. 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 of the employer mandate would deeply influence a host of state and local public policy decisions as those governments seek to maximize the impact of their improving, but still-tight budgets.

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. at 556-57. *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 seemed to recognize 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 this substantive federalism backstop 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 U.S. 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 applicability of *Garcia*. That is particularly true in a case such as this where even *Garcia* acknowledged a substantive Tenth Amendment backstop where

defects in the political process render the Tenth Amendment a practical nullity.[3] And, here, if nothing else, the IRS has manipulated the political process by adopting a rule contrary to the deal that Congress struck in the ACA, and thereby depriving the States of the bargain that Congress enacted.

C. If The Employer Mandate—Like The Individual Mandate—Is A Tax, It Violates 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*

[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."); *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819) (recognizing constitutional doctrine of intergovernmental tax immunity). 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. To protect *Amici* States' deliberate and reasoned decision 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 purports to rewrite the plain language of the Act and the fundamental deal Congress struck with the States.

Dated: October 3, 2014

Respectfully submitted,

DEREK SCHMIDT
Kansas Attorney General

/s/ Jeffrey A. Chanay
Jeffrey A. Chanay
Chief Deputy Attorney General
Counsel of Record
Stephen R. McAllister
Solicitor General
Dwight R. Carswell
Assistant Attorney General
Memorial Building
120 SW 10th, 2nd Floor
Topeka, Kansas 66612
Telephone: (785) 296-2215
E-mail: jeff.chanay@ag.ks.gov
steve.mcallister@trqlaw.com
dwight.carswell@ag.ks.gov

Counsel for Amici Curiae

CERTIFICATE OF COMPLIANCE

1. This brief complies with the type-volume limitations of Fed. R. App. P. 32(a)(7)(B)(i) and Fed. R. App. P. 29(d) because it contains 6,773 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii) and D.C. Cir. R. 32(a)(1), as calculated by the word-counting function of Microsoft Word 2007.
2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally-spaced typeface—14-point Times New Roman—using Microsoft Word.
3. This brief has been scanned for viruses using Sophos Endpoint Security and Control (version 10.3), and no viruses were detected.
4. The hardcopies of this brief submitted to the Court this day are exact copies of the version submitted electronically.

DATED: October 3, 2014 /s/ Jeffrey A. Chanay

CERTIFICATE OF SERVICE

Pursuant to Federal Rule of Appellate Procedure 25(d), I hereby certify that on this 3rd day of October, 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 District of Columbia 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 thirty paper copies to be delivered by Federal Express to the Clerk's Office.

DATED: October 3, 2014 /s/ Jeffrey A. Chanay