

April 16, 2015

No. 29

No Spoof

States Still Await Answers about Obamacare Exchanges

By Scot K. Vorse*

By the end of June, the Supreme Court will rule on the issue of Obamacare insurance exchange subsidies in *King v. Burwell*, a case that could have significant ramifications for the Affordable Care Act (ACA). In implementing the law, the Internal Revenue Service (IRS) made individuals purchasing health insurance on both state and federally facilitated exchanges eligible for tax credits to offset part of the cost of the insurance. That rule violates the plain text of the Act, which makes such subsidies available only for insurance purchased on exchanges established by the states.

At the Supreme Court's March 4 hearing on the case, Justice Anthony Kennedy asked whether the denial of subsidies might constitute federal coercion of the states:

[F]rom the standpoint of the dynamics of Federalism ... there is something very powerful to the point that if [the challenger's] argument is accepted, the States are being told either create your own Exchange, or we'll send your insurance market into a death spiral.¹

Oklahoma Attorney General Scott Pruitt, in a *Wall Street Journal* op-ed, responded to Justice Kennedy as follows:

In other words, Justice Kennedy was asking, if Congress did in fact condition ObamaCare's tax credits on a state having set up an exchange, does that amount to an unconstitutional coercion of the states? In short: no.²

Pruitt cited a January 2012 letter by insurance and health officials from seven states—Kentucky, Maine, New Mexico, North Dakota, Tennessee, Utah and Virginia—that asked the U.S. Department of Health and Human Services (HHS) for a formal legal opinion explaining the federal government's authority to administer tax credits for insurance premiums on federally facilitated exchanges.³

* Scot K. Vorse is a retired investment banker having spent much of his career at Goldman, Sachs & Co. and is a graduate of Harvard Business School. Mr. Vorse is currently the President of [Vorsetrade](#), a software company based on patent pending technology which uses barter logic and technology used by government entities to reallocate excess assets. He can be followed on Twitter at [@scotrbf](#).

As the letter indicates, these states questioned whether the IRS had the power to issue tax credits in states that decided not to set up their own exchanges. But five of these states—Virginia, Maine, North Dakota, Tennessee, and Utah—nonetheless decided not to set up their own exchanges.

Pruitt's point is especially clear when one considers the background to that letter, as described in my November 2014 CEI paper, "Beyond Gruber: How HHS Flip-Flopped on Federal Exchange Subsidies."⁴ For two years after Obamacare's enactment, HHS helped several states set up their own exchanges, but did almost nothing to establish the federal one. In particular, HHS moved quickly after the law was passed to help state governments develop the tax credit calculators needed to make tax credits available through state-based exchanges. Meanwhile, for nearly two years, it developed its own HealthCare.gov website without any effort to offer tax credits on the federal exchange or to develop a tax credit calculator for its site.

It was only after many states appeared to be leaning against setting up exchanges that the Obama administration changed course and began claiming that the Affordable Care Act allows tax credits for both state and federally facilitated exchanges. Only then did HHS begin developing a tax credit calculator for HealthCare.gov.

But as the deadline for states to set up their own exchanges drew near, they still needed a determination as to whether their residents would receive tax credits through federally facilitated exchanges if the states did not set up their own exchanges. This led to a standoff, as states did not want to decide whether to set up exchanges until they knew HHS' decision, while HHS did not want to decide the federal exchange subsidy issue until it knew the states' decisions. It was against this background that in January 2012 the seven states wrote to HHS, requesting a formal opinion on federal exchange tax credits.

Was the letter serious or a prank? On March 16, Ian Millhiser of the Center for American Progress (CAP) attempted to discredit this letter, claiming it was "satirical," a "prank," "joke," and "spoof," because it closely resembled a letter HHS had sent to the states requesting information on their plans for state exchanges. Millhiser claims that "no state questioned the legality of these tax credits during an Internal Revenue Service rulemaking process." He appears to base these allegations primarily on statements by a "state official who signed the letter, who spoke to ThinkProgress [CAP's blog] on condition of anonymity."⁵ And more recently, the Huffington Post claimed that Alabama state officials never realized that the state might be giving up subsidies when it decided against setting up its own exchange.⁶

However, a close examination of the development of the letter shows that the signing states had serious questions about the availability of subsidies through federal exchanges, and that the letter was a careful effort by them to get answers from HHS.

Shortly after Millhiser made his claims, I requested from the Utah Department of Health all records related to the seven-state letter. I received more than 20 emails

written by or to Norman K. Thurston, who was Director at the Utah Department of Health when the letter was written. According to these emails, Thurston initiated, drafted, coordinated and sent the letter on behalf of Utah and the six other states. (See email 1 in the appendix.)

These emails, several of which are excerpted and numbered in the appendix for easy reference, show a serious and coordinated effort by numerous states to obtain the same type of information from HHS regarding federally established exchanges as they had requested for state-established exchanges. They sought comparable information regarding the state and federal exchanges because of, as the states' letter put it, the "complex nature of the policy decision process at the state level" between the two options.⁷ Notably, the states explicitly asked HHS to explain what authority it had to administer tax credits on federally established exchanges.

A few highlights from Thurston's email exchanges demonstrate the seriousness of the letter. Highlights are referenced by the number of the individual email as it appears in the appendix:

- An initial email outlining the concept of the letter was made available by Thurston to most if not all of the states (2).
- The letter was not quickly thrown together but rather was developed, revised and finalized over a period of several weeks, beginning in late November and ending in early January.
- States were becoming increasingly concerned that HHS had "not provided ANY details to the states about the federal model" (5).
- Seven states signed the letter, and according to one email, officials in at least seven other states supported it to some extent—Arizona, Idaho, Ohio, South Carolina, South Dakota, West Virginia, and Wisconsin (6). Other states also took an interest in it. One executive at the Kansas Insurance Department, for example, said: "[W]e had a call with several HHS people on Monday afternoon and told them we were totally in support of the issues raised in your memo" (7).
- Virginia's signature is particularly noteworthy because it is directly at odds with a Supreme Court amicus brief filed by 22 states and the District of Columbia in support of HHS.⁸ That brief stated: "[C]onspicuously absent is evidence that States contemplated the dramatic consequence of depriving their residents of tax credits ..."⁹ Virginia was the lead state on the brief, but its position is directly contradicted by its signature on the Jan. 2012 letter (1, 8).
- The emails confirm that the states' letter was based, in part, on a letter that HHS first sent to them. However, the states' letter was not as a "spoof" of that letter, but rather "a fairly polite request that CMS [the federal Centers for Medicare and Medicaid Services] put forward a plan to tell us the same information about the federal exchange that they are requesting from us on the state exchanges" (9, 5).

The states were not the only ones with questions. On March 1, 2012, a few weeks after the states sent their letter, then-HHS Secretary Kathleen Sebelius testified before the House Subcommittee on Health of the Energy and Commerce Committee. Rep. Joseph Pitts (R-Penn.) submitted several questions to Sebelius, for inclusion in the hearing record, regarding HHS authority to allocate subsidies on federal exchanges. Her answers did little more than reference the IRS.¹⁰ Regardless of whether one views her answers as satisfactory, the fact that she was questioned about the federal exchange subsidies makes it clear they were already an issue for many of the states at that time.

Conclusion. Several states and Members of Congress continued to question the validity of federal exchange tax credits. Some commenters now argue that this question never really came up. But it did, and it is up to the Supreme Court to finally answer it.¹¹

Notes

¹ Scott Pruitt, “A State Reply to Justice Kennedy,” *Wall Street Journal*, March 5, 2015, <http://www.wsj.com/articles/scott-pruitt-a-state-reply-to-justice-kennedy-1425513344?KEYWORDS=scott+pruitt>.

² Ibid.

³ “State Consultation on the Development of a Federal Exchange,” https://cei.org/sites/default/files/State%20Consultation%20on%20the%20Development%20of%20a%20Federal%20Exchange_0.pdf. This document was accompanied by a cover email from the head of Utah’s Office of Health Care Statistics, listing the officials from the various states on whose behalf the document was sent. See email 1 in the email Appendix.

⁴ Scot K. Vorse, “Beyond Gruber: How HHS Flipped on Federal Exchange Subsidies,” *Web Memo* No. 28, November 20, 2014, <https://cei.org/content/beyond-gruber-how-hhs-flip-flopped-federal-exchange-subsidies>.

⁵ Ian Millhiser, “Lawyer Attempting to Cripple Obamacare Cites Satirical Letter to Support his Supreme Court Case,” *ThinkProgress*, March 16, 2015, http://thinkprogress.org/justice/2015/03/16/3633684/oops-anti-obamacare-lawyer-cites-satirical-letter-evidence-supporting-supreme-court-case/?utm_source=newsletter&utm_medium=email&utm_campaign=tptop3.

⁶ Jeffrey Young, “A Case Study on Why the Obamacare Lawsuit Is Based on Mythical History,” *Huffington Post*, http://www.huffingtonpost.com/2015/04/06/alabama-obamacare-supreme-court_n_6999798.html.

⁷ “State Consultation on the Development of a Federal Exchange.”

⁸ Amicus Brief of Virginia et al. in Support of Affirmance, filed January 28, 2015, http://www.americanbar.org/content/dam/aba/publications/supreme_court_preview/BriefsV5/14-114_amicus_affirm_va.authcheckdam.pdf.

⁹ Ibid., p.16.

¹⁰ Hearing before the Subcommittee on Health of the Committee on Energy and Commerce, 112th Congress, 2nd Session, Serial No. 112–121, March 1, 2012, pp. 58–59, <http://democrats.energycommerce.house.gov/sites/default/files/documents/Final-Transcript-Health-FY-2013-HHS-Budget-2012-3-1.pdf>.

¹¹ The CEI paper that cites the states’ letter (see note 4) is referenced in the Amicus Brief of Administrative and Constitutional Law Professors in Support of Petitioners, filed December 29, 2014, p. 27, http://www.americanbar.org/content/dam/aba/publications/supreme_court_preview/BriefsV4/14-114_amicus_pet_lawprofessors.authcheckdam.pdf.

Appendix

For ease of presentation, these emails have been cut, pasted, and formatted onto a single document. Key portions have been highlighted.

Email 1

From: "Norman Thurston"

Date: Wed, 11 Jan 2012 09:39:59 -0600

Subject: Federal Exchange Certification

To: amanda.cowley@cms.hhs.gov, Steven.Larsen@cms.hhs.gov, teresa.decaro@cms.hhs.gov, Teresa.Miller@cms.hhs.gov, timothy.hill@cms.hhs.gov

Cc: katherine.harkins@cms.hhs.gov, susan.lumsden@cms.hhs.gov, Bill.Hazel@governor.virginia.gov, Molly.Huffstetler@governor.virginia.gov, Allyn.Moushey@hhs.gov, Chiquita.Brooks-LaSure@hhs.gov, Doyle.Forrestal@hhs.gov, marguerite.salazar@hhs.gov, Paul.Dioguardi@hhs.gov, william.nold@ky.gov, katrin.teel@maine.gov, rlternes@nd.gov, Dan.Derksen@state.nm.us, brian.haile@tn.gov, Darin.J.Gordon@tn.gov

Dear Mr. Larsen & CCIIO Colleagues,

The Affordable Care Act (ACA) directs the Secretary of Health and Human Services (HHS) to facilitate the establishment of an Exchange in any state that does not achieve certification by January 1, 2013. HHS has published a draft application for that certification form under the Paperwork Reduction Act.

We wish to emphasize to our partners in HHS that it is equally important for states to understand the nature of the federal alternative that will be facilitated if they do not seek certification. In fact, due to the complex nature of the policy decision process at the state level, states need this information much sooner than the January 1, 2013 deadline required of states requesting certification.

We request the following information from HHS no later than June 1, 2012 in order for us to make an informed decision about the direction we should pursue. This deadline is necessary to allow states that are considering deferring some (or all) functions of the exchange to HHS to understand how those processes would work in the context of a state exchange. This information request is based on the certification form proposed by HHS for states. It seems reasonable that HHS be able to provide the same type of information to states as the states would be required to provide to HHS.

Sincerely,

Norman Thurston, Health Reform Implementation Coordinator, State of Utah
Darin Gordon, TennCare Director and Deputy Commissioner, Tennessee Division of Health Care Finance & Administration
Brian Haile, Director, Tennessee Insurance Exchange Planning Initiative
William Nold, Director, Kentucky Department of Insurance
Katrin Teel, Senior Health Policy Adviser, State of Maine Governor's Office
Dan Derksen, Director, New Mexico Office of Health Reform
Molly Huffstetler, Deputy Director, Virginia Health Reform Initiative
Adam Hamm, Insurance Commissioner, State of North Dakota

Norman K Thurston, Ph.D.
Health Reform Implementation Coordinator
State of Utah
PO Box 141000
Salt Lake City, Utah 84114-1000

Email 2

From: **Norman Thurston** <nthurston@utah.gov>
Date: Mon, Nov 28, 2011 at 3:32 PM
Subject: Exchange Certification
To: exchangers@list.nashp.org

It almost escaped my attention, but today some staff and I were reviewing the proposed certification forms. If you haven't looked at it, I would encourage you to do so, and comment if you feel include.

As we were discussing, a thought crossed our minds - Will HHS be willing to provide that level of detail to us about the federal model by mid to late 2012 so we can decide which route to pursue? What would they do if we sent them the same "calendar" of questions and asked them, "Please answer the following questions about the federal model."

One touch of irony - Can they include some legal opinions about whether they have the authority to do what they are proposing to do, just like they are asking from the states?

Is anyone interested in broaching this topic with them in a polite way, of course, but just as another opportunity to highlight that the states also need the same level of disclosure as they would be asking from us, and probably in even tighter timelines?

Email 3

From: Norman Thurston [NTHURSTON@utah.gov]
Sent: Friday, December 23, 2011 9:30 AM
To: Brian Haile
Subject: Federal Exchange Requirements

Dear State Exchange colleagues,

As you may have seen through the Exchangers listserv, I have been working on a document to send to HHS detailing the states' need for information about the federal exchange.

The current (and nearly final) draft is attached. Your comments are welcome.

I would like to send this to our friends at HHS around January 5, 2012, and would like to include as many names of state partners as possible on the e-mail.

Would you let me know if I can include your name and if there is anyone else from your state that would be interested in having their name listed?

Thanks,

Norm

P.S. I apologize for sending this out as a mass bcc: e-mail, but I wanted to limit distribution to only state friends and the listserves seem to have gone beyond where I feel comfortable. While I have a decent list, I do not necessarily have everyone that may be interested. Please do not assume that others in your state are on my list. Feel free to circulate within your state.

Norman K Thurston, Ph.D.
Health Reform Implementation Coordinator
State of Utah

Email 4

From: **Norman Thurston** <nthurston@utah.gov>

Date: Tue, Dec 27, 2011 at 12:09 PM

Subject: RE: Federal Exchange Requirements (Auto-Reply: Vacation notice)

To: "Haile, Brian" <Brian.Haile@tn.gov>

>>> Brian Haile <Brian.Haile@tn.gov> 12/27/11 12:08 >>>

Norm,

Please include my name and affiliation. I will ask Darin if he wants to sign on -- but I won't see him until the 4th, so I may not be able to get back with you in time.

Here are a few thoughts and additional questions below, which may or may not be worth including. I completely understand if the ship has sailed and you are unable to make changes at this point.

Thanks for doing this -- I really like the concept and want to be supportive in any way that I can!

Best,
Brian

Add'l Questions on Federal Certification Process

State Policy Options

1. What is the process that the federal government will use to establish or modify rating areas (pursuant to 42 USC § 300gg(a)(2)) if the respective state has no definition in state statute or regulation?
2. If the Governor provides written notice to the Secretary of HHS regarding the State's definition of rating areas, under what conditions (and using which specific legal authorities) would the federal government use to overrule the State's policy as embodied in the Governor's notice?
3. If the Governor provides written notice to the Secretary of HHS that the state elects to define "small group" as 50 or fewer employees pursuant to 42 USC § 18014(b)(3), under what conditions (and using which specific legal authorities) would the federal government use to overrule the State's election as embodied in the Governor's notice?
4. If the Governor provides written notice to the Secretary of HHS regarding the State's definition permissible rating practices (with respect to allowable variation based on age, tobacco use, and rating area), under what conditions (and using which specific legal authorities) would the federal government use to overrule the State's policy as embodied in the Governor's notice -- presuming that the rating practices are equal to or less than the maximum variations permitted under PHSA Section 2701(a) as added by PPACA Section 1201(4)? For example, if the Governor were to notify the Secretary that qualified health plans could vary premiums by a maximum of 10% (or a ratio of 1.0:1.1) on the basis of tobacco use or by a maximum of 20% (or a ratio of 1.0:1.2) on the basis of age, how would the federal government respond?
5. How will the federal government enforce and collect the state financial liabilities associated with benefit mandates in the individual market that may exceed the EHB standard (pursuant 42 USC § 18031(d)(3)(B))?

Qualified Health Plans

6. What specific contracting standards for qualified health plans will the federal government use with respect to provider network adequacy standards? Also, how will the federal government define services areas -- and how may these differ and/or interact with respect to rating areas? Please provide a detailed description of such standards by provider type and by urban, suburban, and rural areas.
7. To what extent would a federally-facilitated exchange allow issuers to vary network by metallic tier?

8. With respect to out-of-network service delivery, will the federally-facilitated exchange require qualified health plans to cover urgent and emergency services at specified or minimum reimbursement levels? If so, how will the federally-facilitated exchange define such reimbursement levels?
9. What accreditation requirements will federally-facilitated exchanges require of qualified health plans?
10. How will federally-facilitated exchanges conduct independent rate reviews for qualified health plans, which are apparently separate and apart from those performed by state regulators, without compromising state regulatory authority?
11. In what specific ways will the federally-facilitated exchange avoid the early Medicare Part D experience and better ensure that consumers have a more manageable number of benefit options from which to choose? On a related note, to what extent will the federally-facilitated exchange seek to standardize benefit designs among qualified health plans akin to the approach used in the Medicare Supplement program?

Exchange Operations

12. How will the federal government operationalize the "employee choice" models in the SHOP exchange -- and under what conditions and using what legal authorities will the federal government allow federally-facilitated SHOP exchanges to provide more options for employee choice than the minimum described under PPACA Section 1312(a)?
13. Using which specific legal authorities would the federal government compel states to share income tax, professional privilege tax, property tax, unemployment compensation, and other financial data with a federally-facilitated exchange? Please describe how this may work -- and how the federally-facilitated exchange would incorporate these data elements in the eligibility determination process?
14. How will the federally-facilitated exchanges collect and remit premium taxes to state governments as and if required by state law?
15. How will the federal government evaluate the funding "requirements" for Navigator programs and establish an overall budget for such activities in each state in which a federally-facilitated exchange is operating?
16. How will the federally-facilitated SHOP exchange define and enforce participation and employer contributions within the small group market?
17. To what extent will the federally-facilitated SHOP exchange screen and determine eligibility for Medicaid, CHIP and premium tax credits for employees that may be eligible? Please describe in detail the business process that the federally-facilitated exchange will use for this purpose.

Miscellaneous

18. Under what circumstances would the federal government operate a Basic Health Program and standard health plans within a federally-facilitated exchange?
19. What types of marketing parameters or restrictions would the federally-facilitated exchange include in its contracts with qualified health plans -- and what specific mechanisms (e.g., liquidated damages, etc.) would the federally-facilitated exchange monitor and enforce such requirements?

Email 5

From: **Cathy Dupont** <CDUPONT@utah.gov>
Date: Mon, Nov 28, 2011 at 9:28 AM
Subject: Re: Fwd: CCIIO - State Exchange Update - November 25, 2011
To: "Thurston, Norman" <nthurston@utah.gov>

Norm;

The application for states to submit to the feds to get the American Health Benefit Exchange "certified" by the feds is interesting...are the feds going to provide that level of detail to the states about the federal model before 2013 so we can decide whether we want to tell the feds we will run our own exchange , or tell them to "stuff it" (in the spirit of Thanksgiving) and run their own exchange????? It really gets my blood boiling when the feds ask the states for so much and they have not provided ANY details to the states about the federal model. Wonder what the feds would do if all the states sent the feds the same "calendar" of questions and said "Please answer the following questions about the federal model (including legal opinions that they really have the authority- like they ask for from the states). Why should the states be asked for info the feds are not even able or willing to give back to the states?"

Cathy

Email 6

From: **Norman Thurston** <nthurston@utah.gov>
Date: Thu, Jan 12, 2012 at 8:23 AM
Subject: Re: Fwd: Federal Exchange Certification
To: KDrobac@nga.org

The signers were UT, TN, KY, VA, NM, ND, ME. The supportive non-signers include OH, WV, SD, SC, ID, AZ, and WI. Some of them will express their support informally as they get permission.

I also heard back from WY, IN, and OK but they specifically give support.

Please don't circulate this list.

Email 7

From: **Norman Thurston** <Nthurston@utah.gov>
Date: Wed, Jan 11, 2012 at 9:05 AM
Subject: Re: Federal Exchange Certification
To: LJShep@ksinsurance.org

Thank you!

>>> Linda Sheppard 01/11/12 9:05 AM >>>

Norm, we had a call with several HHS people on Monday afternoon and told them we were totally in support of the issues raised in your memo.

Email 8

From: **Norman Thurston** <NTHURSTON@utah.gov>
Date: Thu, Jan 5, 2012 at 11:24 AM
Subject: Fwd: Federal Exchange Certification
To: Bill.Hazel@governor.virginia.gov, Cindi.Jones@governor.virginia.gov

Bill,

Can I include you (or someone else from VA) on the sender list?

Email 9

From: **Norman Thurston** <nthurston@utah.gov>

Date: Mon, Dec 5, 2011 at 8:28 AM

Subject: Federal Exchange "Certification" Process

To: Penny.Schwiebert@doi.idaho.gov, NicolePJ@health.ok.gov,

Carrie.Haughawout@insurance.ohio.gov, Brian.Haile@tn.gov

Cc: "Dupont, Cathy" <CDUPONT@utah.gov>

Assuming that my time holds out, I think what I would do is draft a memo similar to the Technical Manifesto using their application form as a base. I would outline a fairly polite request that CMS put forward a plan to tell us the same information about the federal exchange that they are requesting from us on the state exchanges. I don't think I will go so far as to create a form, just outline a detailed list of elements that we need to see. The most important piece would be the timeline that they have in mind, and I would emphasize that we need it sooner rather than later.

I hope to have a copy for circulation in the next day or so.