Testimony before the Subcommittee on Energy Policy, Health Care and Entitlements of the House Committee on Oversight and Government Reform

Oversight of IRS's Legal Basis for Expanding Obamacare's Taxes and Subsidies

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Dear Chairman Lankford, Ranking Member Speier, and Members of the Subcommittee,

Thank you for providing a forum where I may present my concerns regarding the regulations enacted by the IRS and Department of Health and Human Services to implement the Affordable Care Act ("ACA"). The Department of Health and Human Services defines an exchange to include any state-established or federally-facilitated health insurance exchange, and the IRS adopted the Department's definition for its entire set of regulations implementing the ACA. This definition overlooks the critical differences between state-established and federally-facilitated exchanges under the ACA's subsidy provisions in Section 36B of the Internal Revenue Code. The statute provides subsidies for certain individuals who buy insurance on a state-established exchange but not on a federally-facilitated exchange. These subsidies have significance outside of just spending taxpayers' money: the federal government's payment of a subsidy may trigger a substantial penalty for the payee's employer. The State of Oklahoma's decision—as well as decisions by 34 other states—not to establish an exchange should have prevented substantial federal spending as well as significant compliance costs both for the states as employers and for private employers. The conflict between the statute's provisions and the IRS's definitions led to my office choosing to litigate the matter, and it warrants your concern.

The ACA's Exchanges, Subsidies, and "Shared Responsibilities"

Title I, Subtitle D, Parts II and III of the ACA call for the creation and operation of markets, referred to in the Act as "Exchanges," where individuals may purchase health insurance. Section 1311 of the ACA provides for the establishment of an Exchange by a State. 21. Section 1321(c) of the ACA provides for a federally-facilitated Exchange.

In the case of an individual who meets certain criteria including a household income requirement, Title I, Subtitle E, Part I, Subparts A and B of the ACA effectively provide for subsidizing that individual’s health insurance coverage if the individual purchases it on an Exchange established by a State. The subsidy consists of an “advance payment” from the Treasury under the conditions established in Sections 1401, 1411 and 1412 of the Act to the issuer of the health insurance coverage. The Treasury makes the advance payment in an amount equal to an estimate by the Exchange of the size of the tax credit to be taken against the payee’s income tax under Section 36B of the Internal Revenue Code. Section 36B(b) provides a formula for computing the amount of the Premium Tax Credit for each month of the taxable year.

Section 1501 of the ACA added Section 4980H to the Internal Revenue Code. Section 4980H potentially applies to any “applicable large employer,” defined as an employer that employed on average 50 or more full-time equivalent employees on business days during the prior year. The requirements imposed on a large employer under Section 4980H trigger if and only if an “advance payment” has been or could have been made or a “premium tax credit” has been or could be allowed to or on behalf of one of the employer’s full time employees. When Section 4980H triggers with respect to a large employer, it imposes a significant assessment that may be as much as $2,000 for every full-time employee at the company less a thirty employee allowance. The only way the employer may avoid the payment is to have arranged in advance to make available insurance coverage to full-time employees and their dependents. The insurance must provide “minimum essential coverage” that meets a regulation-set “minimum value” through an “eligible employer-sponsored plan” at a cost satisfying standards of “affordability” under the Act. In addition, the Act imposes other significant obligations such as detailed reporting requirements on employees.

Section 4980H thus imposes significant compliance costs and possibly even direct payment obligations on employers. Yet Section 4980H only triggers when the Treasury makes an advance payment or an individual takes a premium tax credit. Under the ACA, these events should only occur when individuals purchase insurance on an Exchange established by a State.

The IRS Regulation and Oklahoma's Litigation

On May 18, 2012, Treasury issued a final regulation that incorporated the definition of "Exchange" found in final regulations issued by the Department of Health and Human Services on March 25, 2012. The Department of Health and Human Services defines "Exchange" to include a federally-facilitated Exchange, which would be broader than just the category of State-established Exchanges. Thus, the Treasury can be expected to permit advance payments on behalf of individuals who have not enrolled in insurance through an Exchange established by a State. Further, the Treasury and the IRS can be expected to permit some individuals to take premium tax credits under Section 36B of the Internal Revenue Code despite not having enrolled in insurance through a State-established Exchange.

Not only does this result conflict with the ACA, but the regulators ignored public comment pointing the problem out. Public comments in response to the proposed regulations stated clearly that the regulations would cause advance payments to be made and premium tax credits to be allowed even if individuals only had coverage through federally-facilitated exchanges. For example, one comment noted that

> [n]owhere within the [statute] is an Exchange created under Section 1321 mentioned regarding eligibility of the premium tax credit. Again, the IRS does not have the authority to expand access to a premium tax credit beyond what is clearly written within PPACA.

The Treasury brushed aside critical comments with only the most cursory analysis. Nowhere does the notice indicate that the Treasury considered contrary evidence or legal considerations. Thus, the Treasury's regulation appears geared more toward enacting the agency's own policies than acting as a faithful agent of Congress.

My office had previously filed a lawsuit against various officials in the federal government out of concerns that the ACA contained unconstitutional provisions and conflicted with the Oklahoma Constitution's guarantee that a person may not be coerced into participation in any health care system. While the United States Supreme Court's opinion in *National Federation of Independent Business v. Sebelius* dealt with some of the issues raised by my office, the IRS's flawed, unconsidered regulations became final after the Supreme Court had already begun deliberation. Fortunately, because my office did not join the larger set of lawsuits before the Supreme Court last year, we had the opportunity to amend our complaint on September 19, 2012, to obtain relief. Rather than correct its improper regulations, the federal government moved to dismiss the State of Oklahoma's complaint. The outcome of that motion is currently pending in district court in the Eastern District of Oklahoma.

We have also filed a notice to the court concerning the administration's recent decision to delay implementation of Section 4980H for a year. The administration's justification for the delay cited numerous complaints from employers about the burdens imposed on them by the ACA. The delay therefore confirms my office's concerns: exactly where these burdens fall is a serious matter, and if the ACA exempts employers in states foregoing the establishment of their own Exchanges, that exemption should be recognized and enforced. The ACA represents one of the most sweeping reforms of an entire corner of American industry—actually, American life—ever contained in one bill. Regulators implementing such a broad statute should not take limitations imposed by Congress lightly. We hope to obtain relief through the justice system, but we also welcome Congressional oversight being brought to bear on these agencies.

Thank you for affording me the opportunity to present these concerns. Please see attached some of our key filings from the litigation, including our amended complaint, our response to the federal government's motion to dismiss, and notices we have filed with the court.

E. SCOTT PRUITT
ATTORNEY GENERAL OF OKLAHOMA

About Scott Pruitt

Attorney General E. Scott Pruitt was elected as the 17th Attorney General of the State of Oklahoma on November 2, 2010. He is the second Republican in the history of the state to hold the office, which oversees 80 attorneys. He is dedicated to fighting corruption, protecting Oklahoma’s vulnerable citizens, championing public safety measures to reduce violent crime and advocating excellence in the administration of the law, justice and protecting the interests of the Great State of Oklahoma and its citizens.

Attorney General Pruitt has quickly risen as a national leader in the cause of restoring limited government and the proper balance of power between the states and the federal government. As a first priority in office, Attorney General Pruitt established Oklahoma’s first Federalism Unit in the Office of Solicitor General to more effectively combat unwarranted regulation and systematic overreach by federal agencies, boards and offices.

Pruitt currently serves as chairman of the Republican Attorneys General Association (RAGA) and chairman of the Midwest Region of the National Association of Attorneys General (NAAG). Under his leadership, attorneys general have come together to advance policies and legal strategies that protect the interests of their states from an overly intrusive federal government, with a particular focus on domestic energy security and production. Attorney General Pruitt has led the charge with repeated notices and subsequent lawsuits against the U.S. Environmental Protection Agency for their leadership’s activist agenda and refusal to follow the law.

Attorney General Pruitt is an ardent defender of Oklahoma consumers, families and children in his capacity as Oklahoma’s top law officer. During his first months in office, he transformed the AG’s consumer protection efforts into the Public Protection Unit with a broader focus on keeping citizens safe. He established the Internet Crimes Against Children Unit to provide specific training for investigators and expanded resources for tracking criminals who intend to exploit children through technology.

In response to a personal call to defend the needs of children who are less fortunate, Attorney General Pruitt worked to negotiate a state settlement through the Department of Human Services that will dramatically improve foster care in Oklahoma. He was awarded the “Hero Award” by the Marland Children’s Home for his efforts to prevent closure of the home and eviction of children who are emotionally disabled. In 2011, Attorney General Pruitt received the Humanitarian Award by Oklahoma CARE, a coalition of ministries and providers who deliver care for troubled children and their families.

Establishing and respecting the Rule of Law is a hallmark of Attorney General Pruitt’s administration. In late 2011, Attorney General Pruitt made national headlines when he took the bold step of negotiating an Oklahoma settlement with mortgage servicers instead of joining a 49-state mortgage settlement that exceeded the proper legal role and scope of authority vested in state attorneys general. The Oklahoma agreement with several of the nation’s largest mortgage service providers included $18.6 million in compensatory damages for Oklahomans who were harmed by unfair practices during the foreclosure process.

Before being elected Attorney General, Pruitt served Broken Arrow, Coweta and Tulsa in the Oklahoma State Senate where he served for eight years, four of those as Assistant Republican Floor Leader. In the Senate, he was the leading spokesman for workers' compensation reform, lawsuit reform and greater accountability for government spending. He championed traditional, faith-based legislation that included allowing faith-based organizations to partner with the state in helping prisoners successfully re-integrate into society after their sentences were fulfilled.

Attorney General Pruitt used his experience in the Legislature to transform the AG's Workers' Compensation and Insurance Fraud Unit and the Medicaid Fraud Control Unit. Under his leadership, the fraud units increased prosecutions, hired 12 investigators, secured more than $20 million in Medicaid fraud restitution and worked directly with Oklahoma businesses to educate workers on fraud recognition and reporting.

Attorney General Pruitt's record of defending religious freedoms began during his time in the state Legislature with his efforts to author and successfully pass the Religious Freedoms Act, making Oklahoma one of the first states to pass an act that makes it more difficult for a government to burden an individual's right to practice their faith, especially in public. His efforts continue as Attorney General, joining six states to fight the federal health care mandate that will require religious groups to violate their beliefs. In 2012, Pruitt was selected to serve as a trustee for The Southern Baptist Theological Seminary.

From 2003 to 2010, Attorney General Pruitt was co-owner and managing general partner of the Oklahoma City Redhawks, the Triple-A baseball team in Oklahoma City. The team, under his leadership, regularly rated among the league's leaders in attendance and merchandise sales.

Pruitt grew up in Lexington, Kentucky, where he graduated high school and earned a scholarship to play baseball as a second baseman at the University of Kentucky. He earned a bachelor's degree in communications and political science at Georgetown College before being accepted to the University of Tulsa College of Law. After working his way through law school and earning a Juris Doctorate, Pruitt ventured into private practice, specializing in constitutional and employment law.

The Attorney General and his wife of 22 years, Marlyn, are raising two children, McKenna and Cade, in Tulsa. The Pruitts are members of the First Baptist Church of Broken Arrow, where Pruitt serves as deacon.