State believes Hoosiers aren't eligible for tax credits under Obamacare

Maureen Groppe
October 13, 2013

When Indiana decided last year not to run its own health exchange under Obamacare, Gov. Mike Pence said it was because the move would cost the state too much money without providing enough benefits.

The state revealed for the first time in a lawsuit filed this week that it also assumed that by opting for the federal health exchange that Hoosiers would not receive the federal tax credits designed to help needy people afford health insurance.

That, in turn, would prevent large employers in the state from being penalized under the health-care law for not providing insurance to workers, the lawsuit argues.

The lawsuit was filed Tuesday by Indiana Attorney General Greg Zoeller. He said he teamed up with 15 school corporations to argue that the Internal Revenue Service lacks authority to penalize the state and other Indiana employers for not offering coverage to anyone working at least 30 hours a week. The threat of the penalties is causing the state and schools to cut the hours of some employees because they can't afford to pay for their health insurance, Zoeller said.

The suit attacks a part of the law that some have described as sloppy wording but that critics say was intentionally written so tax credits would be available only in states that run their own exchanges. Although lawmakers expected most states would want to run the exchanges - because states regulate their own insurance markets - most states decided not to.

Legal challenges

Suits similar to Indiana's have been brought by Oklahoma's attorney general and a group of small-business owners and individuals in six states. If the suits are successful, they would undermine one of two main ways that authors of the 2010 health-care law designed it to make insurance available to millions more people than are covered now. About 13 percent of Hoosiers - more than 800,000 people - lack insurance.

The law as originally written required states to expand their Medicaid rolls - to include households earning up to 138 percent of the federal poverty level - with the federal government picking up most of the cost. But after Indiana and other states challenged the law, the Supreme

Court ruled last year that states can choose not to go along with the Medicaid expansion. That was Indiana's choice.

The second main change designed to increase the number of insured Americans was the creation of the exchanges for people who don't get insurance through an employer or a government program such as Medicare or Medicaid. The exchanges are regulated marketplaces that allow consumers to compare plans and find out whether they qualify for a tax credit to reduce the price of a premium.

About 178,000 Hoosiers now buy insurance on their own. An additional 344,000 - most of whom lack insurance - could enter the individual market through the exchange. Most are expected to qualify for a subsidy, available to those earning 100 to 400 percent of the federal poverty level - about $24,000 to $94,000 per year for a family of four.

The law requires most people to have insurance, starting next year, or pay a penalty. Beginning in 2015, businesses with at least 50 full-time employees that don't offer affordable coverage face a penalty if any worker purchases insurance on the exchange with the help of a tax credit. Full time is defined as working at least 30 hours a week.

Cutting hours

"The costly and burdensome employer mandate the IRS wrongly applies to government employers such as our school corporation interferes with our ability to efficiently manage our workforce," said Randy Taylor, assistant superintendent of Martinsville Schools.

The district is among those that have cut the hours of instructional aides to fewer than 30 hours a week, saying school budgets aren't large enough to pay for the aides' health insurance.

The state's suit argues that schools and other Indiana employers shouldn't be subject to penalties because of the way different sections of the Affordable Care Act reference the exchanges.

One part of the law (Section 1311) says states must create an exchange by 2014. Another part (Section 1321) says that if a state doesn't create an exchange, the federal government will operate it.

When the law refers to the tax credits available on the exchange, it references Section 1311, which talks about state-backed exchanges, and not to Section 1321, which talks about the federal fallback option.

As a result, the subsidies are available only on state-run exchanges, contrary to how the IRS has interpreted the law, Indiana officials say.

"By authorizing federal premium-assistance subsidies to individuals who do not qualify under the statute, the IRS rule exceeds the agency's statutory authority and is arbitrary, capricious and contrary to law," Zoeller wrote in the suit.

If Hoosiers can't receive premium subsidies, then Indiana employers can't be penalized for a worker who receives a subsidy, Zoeller continues.

This issue was raised by opponents of the law when the IRS published its rules for administering the tax credits and employer penalties. The IRS said the law and legislative history support its interpretation.

Subsidies intended

The nonpartisan Congressional Budget Office and Joint Committee on Taxation also concluded that subsidies are available on federally run exchanges.

Senate Democrats involved in the writing of the law have told NPR and other media outlets that the intent was for subsidies to be available on all the exchanges.

"That's what everybody in Congress assumed that they were voting on when they voted for the Affordable Care Act," said Timothy Jost, an expert on health law at Washington and Lee University.

Jost said other sections of the law make it clear that subsidies are available on all the exchanges.

But Jonathan Adler, a law professor and director of the Center for Business Law and Regulation at Case Western Reserve University, and Michael Cannon, director of health policy studies at the Cato Institute, argue that there's a "gaping hole" in the law's regulatory scheme.

"Our further research demonstrates that this feature was intentional and purposeful and that the IRS's rule has no basis in law," the pair wrote in an article published in Health Matrix: Journal of Law-Medicine.

Indiana's deliberations on whether to run its own exchange began with then-Gov. Mitch Daniels, who accepted $7.9 million in federal funds to explore the option. Daniels ultimately deferred the decision to his successor, knowing he would leave office before the exchange started.

After the November election, then Gov.-elect Pence told Daniels that running the exchange would cost millions of dollars without giving Hoosiers more control over health-care choices or lower premiums.

But he didn't say at that time, as the lawsuit does, that the state assumed not running an exchange would block the tax credits.

Pence spokeswoman Christy Denault didn't directly respond to questions about why the tax credits weren't mentioned previously. But she said in an email that the governor supports the lawsuit's efforts to protect the state from the "job-killing employer mandates and IRS fines that are part and parcel of Obamacare."

Zoeller wrote in the lawsuit that "by not creating an exchange, the use of which may trigger financial penalties for employers, a state can create a more hospitable business environment for large employers."