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How a Drafting Error Could Liberate States from Obamacare's Employer Mandate

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Today's *Politico* contains a profile of two free-market health wonks—my co-blogger, John R. Graham, and Michael Cannon of the Cato Institute—who have been waging an all-out campaign to persuade Republican-run states not to implement the Affordable Care Act's subsidized insurance exchanges. John and Mike appear to be succeeding, and not all Republicans are pleased. But the *Politico* report buries the big story in all of this: that a critical drafting error in Obamacare may liberate states from the law's provision that forces employers to provide health insurance to most of their workers.

Last summer, I highlighted this intra-conservative debate on Obamacare's insurance exchanges. John had posted an article lambasting the pre-Obamacare insurance exchange in Utah, which was implemented by Republicans. Norm Thurston, who designed the Utah exchange under then-Gov. Bob Herbert (R.), penned a rebuttal. "Doing nothing is probably the worst thing any state can do to prevent federal action," Norm argued. "The best way for all states to prevent federal intrusion is to make health system reform a states' rights issue."

Norm's argument is echoed in the *Politico* piece by Alabama state representative Greg Wren (R.) and Leavitt Partners insurance-exchange guru Cheryl Smith. Graham and Cannon "have targeted…leadership, [and] committee chairs [in the state legislatures]," Wren grouses. "Oftentimes, people in those positions can stop or speed-bump any kind of legislation."

Pro-exchange Republicans fear federal intrusion

The key Republican argument in favor of setting up the exchanges had been that Obamacare allows the federal government to set up its own exchanges, if states don't comply with the new law. Pro-exchange Republicans, at the state level, believed that if

they set up the exchanges themselves, they could do so in a more market-oriented way than the federal government would.

However, in September, David Hogberg discovered that, due to a drafting error in the law, people who signed up for insurance in the federally-run exchanges would not be eligible for Obamacare's subsidies. While the Treasury Department has attempted to invent a regulation whereby subsidies could be offered via federally-run exchanges, the Obama administration has no legal authority to do so, and any attempt of that nature would be immediately challenged in the courts.

Feder and Millman, the *Politico* authors, erroneously claim that "most legal experts think that this is a drafting error that the Obama administration can fix through regulation." I'm not sure which legal experts they've polled. But Congress' Joint Committee on Taxation, the non-partisan body that assesses all tax legislation, includes only state-based exchange spending, and not federally-run exchange spending, in its estimates of Obamacare's impact on tax revenue, precisely because the law's language requires it. (Read my September 2011 blog post for a thorough discussion of the issue.)

Cheryl Smith isn't deterred. It "may be right" that the law doesn't allow for subsidies of federally-run exchanges, "but if you're a state policymaker, do you really want to bet the farm on that?" Smith's consulting firm, Leavitt Partners, was founded by another former Republican Governor of Utah, Mike Leavitt, who also served as HHS Secretary under George W. Bush. Leavitt has a substantial business in advising state governments on how to set up exchanges.

Graham and Cannon appear to be winning the argument. "Every time when I go into these states, there are usually a bunch of Republican politicians who have bought this line that creating a state exchange will protect them from Obamacare," says Cannon in the article. "It's fun going in there and telling them, 'No, actually, if you want to protect your state, tell the federal government…it's your stupid law, you implement it."

States that don't set up exchanges will have an economic advantage

Graham and Cannon oppose setting up exchanges for a number of reasons. Their principal argument is one of political economy: setting up exchanges helps give a certain legitimacy and permanency to Obamacare, and creates powerful interest groups (especially insurers) that would strive to block their repeal. "Our approach has to be absolute non-collaboration, civil disobedience—well, not civil disobedience but resistance…by whatever means," John Graham tells *Politico*.

But there's another argument: while the ACA strictly regulates the kinds of insurance plans that are eligible for the exchanges, narrowing consumer choice and plan-design innovation, the law exerts somewhat less control over plans issued *outside* the exchanges. If you have a consumer-driven plan, for example, with a health-savings account and high-deductible insurance, the exchanges won't be as friendly to your setup.

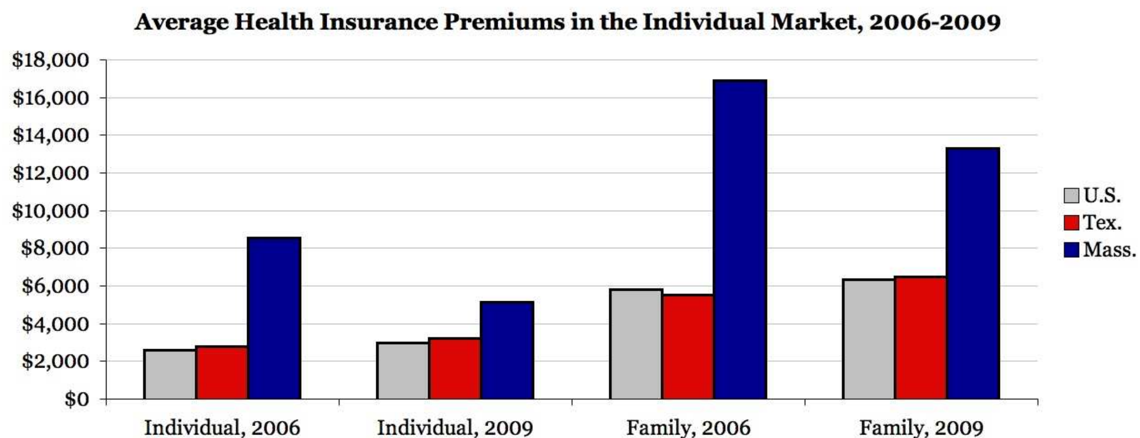
In addition, as *Politico* notes, Cannon argues that "if states don't act, employers will be better positioned to legally challenge penalties they would have to pay if their employees end up getting subsidized coverage in the exchanges." That's because the employer mandate is included in Obamacare so as to prevent companies from dumping all their workers onto the exchanges. Cannon credits Vanderbilt law professor Jim Blumstein with the insight.

The law specifies that the penalties against employers are only triggered when their workers receive "premium assistance" under the exchanges. Section 4980H of the Affordable Care Act reads, in part: "**if** (1) any applicable large employer fails to offer its fulltime employees [eligible insurance coverage], **and** (2) at least one full-time employee of the applicable large employer has been certified…as having enrolled [in an exchange-subsidized insurance plan], **then** there is hereby imposed on the employer an assessable payment." (Emphasis added.)

Hence, those state politicians that aren't as zealously opposed to Obamacare as Graham and Cannon have another reason to oppose the state exchanges. By doing so, they thwart Obamacare's empoyer mandate, thereby lowering the costs of doing business in their states. That, in turn, gives them a competitive economic advantage over states that do set up Obamacare-approved exchanges.

Is there a middle ground?

While I am just as committed to repealing Obamacare as John and Mike are, there is data out of Massachusetts that suggests that exchanges dramatically lower premium costs for people who have to buy insurance for themselves. So, perhaps, there's a middle ground, one that can allow states to reject Obamacare's onerous exchanges in favor of more market-based ones.



The upshot of Obamacare's drafting errors in this area is that states have huge leverage in how they set up their own exchanges. HHS Secretary Kathleen Sebelius can choose not

to certify a particular state exchange, because it doesn't comply with Obamacare's standards. But conservative states could deliberately set up non-compliant, market-oriented exchanges. If HHS didn't certify them, then those states would fail to gain Obamacare's insurance subsidies, but they would also be liberated from the law's employer mandate.

In other words, states could gain the better of both worlds: reduced premium costs through a market-oriented exchange, and elimination of the job-killing employer mandate.

My Manhattan Institute colleague, Paul Howard, has just come out with a policy paper on this very question: what would a market-oriented exchange look like? He points out that, in a liberal state like New York where the government has wrecked the individual insurance market, an exchange could do a lot to increase choice and lower costs.

Paul identifies five key principles for a market-oriented exchange: (1) open competition among a wide variety of plans; (2) granting insurers flexibility in insurance design; (3) making insurance cheaper for younger people by allowing insurers to charge them less (i.e., limiting "community rating"); (4) freedom from political influence; and (5) giving companies the ability to give their workers tax-free money to buy insurance on the exchanges.

Paul's report is extremely detailed, and merits full treatment in a separate blog post. But the bottom line is that people who favor free-market solutions to health care shouldn't dismiss the concept of exchanges. Obamacare's version is poorly designed, costly, and intrusive. The law shows how exchanges can be part of the problem. As Paul demonstrates in his thorough report, however, exchanges can also be part of the solution.

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