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'Exchange' for the Worst

ObamaCare is already proving to be unworkable in state practice.

Democrats promised that health-care reform would be a smooth exercise in expert planning, but so far its "implementation" has been as anarchic and improvisational as the Affordable Care Act's passage. Yet amid the mayhem, there's a chance to mitigate some of the damage.

On the ever-lengthening fiasco list, the "exchange" problem is one of the worst. Congress told states to build these bureaucracies that will dispense health insurance subsidies and regulate coverage, but by and large the states aren't doing so. The National Academy for State Health Policy reports that only 13 states are making "active" progress on their exchange. That means they've checked off five or six of the seven basic boxes that the Health and Human Services Department says they must, like pass legislation or issue an executive order establishing an exchange.

But even progress among these 13 states—home to only about a third of the U.S. population—is an overstatement, given that the exchanges need to be running by October 2013 for coverage in 2014. The National Academy lists 109 specific exchange "milestones." Massachusetts is doing best, and well it should be, given that RomneyCare was such a head start. It has met just 56% of these requirements

California, another liberal leader, is at 44%. Oregon and West Virginia are in the 30s. Illinois, Colorado and Washington state are in the 20s—and then every other state gets much, much worse. Eighteen states have made zero progress and don't want to make more.

Many states run by Republicans are refusing to cooperate as a kind of civil disobedience. But HHS's regulatory and fiscal demands are overloading the bandwidth even in states that support ObamaCare. Vermont is at 19%. New York of all places is at 6%.

The exchanges do not merely subsidize but must verify who is eligible by income and residency, police compliance with the individual mandate and report scofflaws to the Internal Revenue Service; regulate insurers and enforce price controls; and penalize businesses that don't insure their employees. All this is a vast, complex, extremely technical and expensive undertaking that the states can barely handle, even if they wanted to.

To gauge the scale, consider that the IRS inspector general recently reported that ObamaCare "represents the largest set of tax law changes in more than 20 years and affects millions of taxpayers." The IRS needs to hire 1,278 people this year and another 859 in 2013 to usher in the revolution. For comparison, there are only 6,750 U.S. companies that employ more than 2,000 workers.

Our prior advice to anti-ObamaCare states was to ignore the HHS-IRS afflatus and start from scratch, attempting to design clearinghouses that could make the individual and small-business insurance markets function more efficiently and transparently. If 10 or 20 states had banded together on a better model, at least the confrontation with HHS would have been constructive and educational.

But it is too late. The law empowers HHS to impose a federally run exchange, which conservative states will hate far more than their own handiwork. States must prove to HHS by this November—10 days after the election—that they are making progress or else the federal exchange swoops in, and only a handful of states are still trying. In 30 states or more, the feds are now in control.

The intriguing and possibly better news is that, according to ObamaCare's statutory text, only state-run exchanges are allowed to pay subsidies. The IRS and HHS characterize this as a glitch and the result of bad draftsmanship—a "scrivener's error." So they ignored this problem when they wrote up the exchange rules.

Yet in a forthcoming paper in the journal Health Matrix, Jonathan Adler of Case Western and Michael Cannon of the Cato Institute argue persuasively that this omission was intentional. Taking a deep dive into the Congressional record, Messrs. Adler and Cannon argue that Democrats left out federal subsidies as an incentive for states to set up an exchange. The point was to put Governors in the supposedly tough spot of choosing to deny their voters benefits if they didn't set up a state exchange.

A state or a penalized business could decide to sue on the Adler-Cannon argument, though the outcome is far from certain. Some judges are literal, others "textualist," and they may uphold the IRS. But this dispute does erase any urgency for states to lend a hand to the Administration.

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The other lever states have is that a federal exchange is still not a certainty. HHS is grappling with the same implementation problems that states are—and it is out of cash. Democrats appropriated about $1 billion for implementation, split with IRS. But Congress needs to affirmatively give HHS another $750 million next year, which the House so far has refused to do. The White House has been quietly issuing veto threats if Congress refuses to spend such sums, and it may become a major issue this autumn.

We hear more than a few Congressional Republicans are apprehensive about this strategy and want to back down, because Democrats call ObamaCare's subsidies "tax credits" and claim opposing them amounts to a tax increase. But Republicans shouldn't help Democrats overcome their own errors in writing what is still a very unpopular law. If the GOP ends up rolling over, it will become a collaborator in the burgeoning chaos in the states.