EMBARGOED UNTIL 10:30 A.M. 7/31/13

Written Testimony of Emily S. McMahon
Deputy Assistant Secretary for Tax Policy
U.S. Department of the Treasury
Before the House Oversight and Government Reform Subcommittee on Energy, Health Policy and Entitlements

July 31, 2013

Chairman Lankford, Ranking Member Speier, and members of the committee, I appreciate the opportunity to testify regarding the premium tax credit created as part of the Affordable Care Act (ACA).

Background

The ACA established Affordable Insurance Exchanges, also known as Health Insurance Marketplaces, where consumers can choose a private health insurance plan that fits their needs beginning in 2014. To help ensure that this insurance is affordable, Congress also included in the ACA a premium tax credit. It is estimated that, when fully implemented, the ACA will provide premium tax credits to help approximately 20 million Americans afford private health insurance. These premium tax credits may be worth over $4,000 per covered individual each year on average.

On August 17, 2011, the Treasury Department and the IRS issued proposed regulations implementing the premium tax credit under section 36B of the Internal Revenue Code (the Code). Final regulations were issued on May 23, 2012. These regulations provide that the premium tax credit is available to eligible individuals enrolling through all Exchanges, whether directly operated by a state government or a federally-facilitated Exchange operated on behalf of a state.

36B Premium Tax Credit Overview

The premium tax credit is a refundable income tax credit designed to help eligible individuals and families with low or moderate income afford health insurance purchased through an Exchange. The credit is generally available to individuals and families with incomes between 100 percent and 400 percent of the federal poverty level (generally $23,550 to $94,200 for a family of four in 2013) who enroll in coverage purchased through an Exchange and who are not eligible for affordable, comprehensive coverage from another source. The credit may be paid in advance directly to the individual's insurance company, lowering the individual's monthly out-of-pocket premiums. If the credit is paid in advance, the individual will reconcile on his or her tax return the amount paid in advance with the actual credit computed on his or her tax return. The amount of the credit is generally set so as to make a benchmark plan affordable to the individual based on their household income. Individuals who are eligible for a premium tax credit may also be eligible for a cost-sharing reduction, which is designed to make affordable any cost-sharing – such as deductibles or co-payments – an individual may owe in conjunction with their insurance.

Treasury and IRS Regulations Process

It may be helpful to describe the process through which regulations are developed. It is the responsibility of the Treasury Department and the IRS to write regulations to implement the tax laws passed by Congress. In every case, we do so in a careful and thoughtful way, with the goal of implementing the law consistent with congressional intent and resolving any statutory ambiguities in a reasonable manner that gives effect to the purpose of the statute. We follow a standard procedure for drafting, approving, and publishing tax regulations, and our process in this case followed the normal course.

Under our standard procedure, the development of Treasury regulations implementing the Code begins with the IRS Office of Chief Counsel. IRS lawyers review the statute to identify any issues that regulations should address and to develop preliminary resolutions of those issues. The IRS lawyers apply well-established principles of statutory construction and draw on their long experience implementing the Code. The analysis is then shared with tax lawyers from the Treasury Department's Office of Tax Policy (OTP), and the two groups confer about the proper interpretation of the statute, discuss any differences of opinion, and develop a consensus approach.

Under this standard procedure, OTP and IRS lawyers work together to draft proposed regulations, which are published in the Federal Register. The Treasury Department and the IRS solicit public comments on the proposed regulations during an official comment period; and, in many cases, the IRS also holds a public hearing to allow stakeholders to provide feedback in person. IRS and OTP lawyers review any comments they receive and consider whether any of the suggested changes should be adopted. Finally, IRS and OTP lawyers draft a final regulation, which includes responses to any comments and makes modifications to the proposed regulations as necessary. All final tax regulations are signed by the Treasury Department's Assistant Secretary for Tax Policy and the IRS Deputy Commissioner.

The IRS and OTP followed this standard procedure in developing the proposed and final regulations under section 36B. In particular, first the IRS, and then the OTP lawyers, considered the express language of section 36B, as well as other relevant provisions of the ACA. They separately and together concluded that the ACA should be interpreted to provide tax credits to income-eligible individuals enrolling through all Exchanges, whether federally-facilitated or directly operated by a state government. This approach was reflected in the proposed regulations issued in August 2011. We received written and oral comments in response to the proposed regulations – some of which were supportive; others argued for a different interpretation. The IRS and OTP reviewed the issue again, taking the comments into account, and concluded the statute should be interpreted as in the proposed regulations on this point. The Treasury Department and the IRS published final regulations in May 2012 that adopted this view.

Eligibility for Premium Tax Credits

Treasury and IRS believe that the final regulations interpret the statutory language in a manner that is appropriate to its context and consistent with the purpose and structure of the statute as a whole, pursuant to longstanding and well-established principles of statutory construction. This interpretation takes into account the fact that section 36B(f)(3), added by the ACA, requires federally-facilitated Exchanges to report to the IRS data related to eligibility for the premium tax credit and the receipt of advance payments – a requirement that would be pointless unless the enrolling individuals were eligible for the premium tax credit. The regulations also reflect the fact that, where a state chooses not to establish an Exchange pursuant to section 1311 of the ACA, Congress provided in section 1321(c) of the ACA that the Secretary of Health and Human Services (HHS) "shall . . . establish and operate *such* Exchange within the State" to serve the residents of that state. In other words, Congress made the federally-facilitated Exchange the equivalent of a state Exchange in all functional respects, including making qualified individuals eligible for tax credits to purchase insurance through those Exchanges.

I also note that the relevant legislative history does not indicate that Congress intended to limit the premium tax credit to state Exchanges, or, more specifically, to exclude the federally-facilitated Exchange. And finally, the regulations are consistent with the explanation of the ACA released by the non-partisan Congressional Joint Committee on Taxation and with the assumptions made by the Congressional Budget Office in estimating the effects of the ACA. In fact, CBO reaffirmed this point in a December 6, 2012 letter to Chairman Issa in which Director Elmendorf stated: "To the best of our recollection, the possibility that those subsidies would only be available in states that created their own exchanges did not arise during the discussions CBO staff had with a wide range of Congressional staff when the legislation was being considered. Nor was the issue raised during consideration of earlier versions of the legislation in 2009 and 2010, when CBO had anticipated, in its analyses, that the credits would be available in every state."

Conclusion

I understand that some members of this committee will have questions about our legal interpretation. While Treasury appreciates the Committee's important oversight role, it is important to remember that our conclusions also are subject to ongoing, active litigation. In fact, I understand some of those plaintiffs were on the earlier panel. As such, it is important to recognize that only the Justice Department speaks to the Administration's official legal positions as to the merits of our conclusions. I will do what I can to answer the Committee's questions today, subject to the Treasury Department's legitimate confidentiality interests and sensitivities concerning active litigation.

As you know, the Affordable Care Act is projected to provide health coverage for nearly 30 million additional Americans. Together with the Departments of Health and Human Services, Labor, and other agencies throughout the Administration, we are implementing the ACA to build on the progress already made toward better and more affordable coverage. We welcome the opportunity to continue our work with this Committee to achieve these objectives. Thank you, and I look forward to answering your questions.