No. 18-10545

In the United States Court of Appeals for the Fifth Circuit

State of Texas; State of Kansas; State of Louisiana; State of Indiana; State of Wisconsin; State of Nebraska,

Plaintiffs-Appellees / Cross-Appellants,

v.

Charles P. Rettig, in his Official Capacity as Commissioner of Internal Revenue; United States of America; United States Department of Health and Human Services; United States Internal Revenue Service; Alex M. Azar II, Secretary, U.S. Department of Health and Human Services,

Defendants-Appellants / Cross-Appellees.

On Appeal from the United States District Court
for the Northern District of Texas, Wichita Falls Division

PLAINTIFFS-APPELLEES / CROSS-APPELLANTS' REPLY BRIEF

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Introduction

The United States underscores in its response how it is trying to have it both ways. In one breath, the United States asserts (at 1) that the ACA "does not excuse the States from their obligation to account for the [HIPF]."[1] In the next (at 4-5, 44), it asserts that States were never subject to the HIPF. The United States acknowledges (at 1) that "all governmental entities are exempt" from the HIPF, but it tries (at 8) to limit that exemption to a healthcare model that either has not functionally existed for twenty years or that has never been adopted. And the United States asserts (at 37) that the actuarial-soundness requirement is a condition on spending except when it is used to coerce States to pay an unconstitutional tax. Then it is not.

These internal inconsistences arise because the United States asks the Court to read both the HIPF and the actuarial-soundness requirement out of their statutory and regulatory context. Applying well-established law, this Court should look instead at the tax code and Medicaid as they exist post-ACA—with all of their discordant amendments, complicated intersectionalities, and inconvenient facts. As the United States does not dispute, the interaction between Medicaid's actuarial-soundness requirement and the HIPF has forced States to pay hundreds of millions of dollars in taxes on pain of losing billions in Medicaid funding.

This concession demonstrates why the district court erred in rejecting Appellant-States' challenges that the Certification Rule exceeded HHS's statutory

[1] Unless otherwise specified, references in this brief to the United States' arguments are to the Reply and Response Brief filed on February 28, 2020. Defined terms are given the same meaning ascribed in Appellant-States' brief filed on January 29.

authority and was procedurally unlawful under the APA as well as their constitutional challenges to the HIPF itself. As the district court correctly held, the ACA exempts States from paying the HIPF. The Executive's actions to nonetheless impose the HIPF violate the substantive and procedural limitations of the APA. Moreover, the Constitution prohibits the United States from either coercing States into paying the HIPF through the Medicaid program or imposing the HIPF directly upon States.

Argument

I. The Certification Rule Violates the APA.

A. Imposing the HIPF on States through the Certification Rule is substantively unlawful under the APA.

As Appellant-States explained (at 39-40), the Court must examine three questions to determine if the Certification Rule is substantively lawful under the APA: (1) whether Congress delegated to the Executive the authority to determine who will be subject to the HIPF, (2) whether Congress specifically addressed whether States must pay the HIPF, and (3) whether the Executive's decision to impose the HIPF through a twenty-year old regulation without considering the impact of the ACA was arbitrary and capricious.

The United States does not appear to dispute this general standard or that the Certification Rule's legality must be examined under the law post-ACA. *See* U.S. Br. 28-29. Nevertheless, the United States seeks to justify the Rule based entirely on HHS's process in 2002. The Court should reject this view, which "would upend the fundamental principle that regulations should interpret statutes and not the other way around." *Contreras-Bovanegra v. Holder*, 678 F.3d 811, 818 (10th Cir. 2012) (en banc). When there is a "legislative overhaul, agencies should recalibrate their regulations to ensure that they maintain a statutory basis." *Id.* at 818; *see also, e.g.*, *Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 742-43 (1996) (discussing when changed circumstances require alterations to regulations); 1A NORMAN J. SINGER & J.D. SHAMBIE SINGER, SUTHERLAND STATUTORY CONSTRUCTION § 22:35 (7th ed. 2009) (Amendments are "construed as if part of original enactment.") (emphasis omitted). As the United States does not dispute, no such recalibration occurred here in light of the ACA. The result is that the Certification Rule fails all three of the inquiries required by *Chevron, USA, Inc. v. Natural Resource Defense*. *Council*, 467 U.S. 837 (1984).[2]

1. *Chevron "Step 0"*. As an initial matter, the United States professes (at 32) to be confused about Appellant-States' argument regarding the interaction between *Chevron* and the nondelegation doctrine. The United States then makes extended forfeiture and constitutional responses (at 31-35) to an argument it admits (at 31) that Appellant-States did not make. To the extent it was unclear, Appellant-States have asked the Court to consider the breadth of the delegation in 42 U.S.C. § 1396b(m)(2)(A)(iii) in determining whether, under the important-decision doctrine, Congress delegated the authority to impose the HIPF on States to the

[2] To the extent that the United States is arguing (at 31) that it never has an obligation to amend its regulations absent a petition from an affected party, such an assertion is without merit. *Congress* required the Executive to change its regulations when it passed a new statute impacting the scope of the agency's discretion.

Executive. *Gundy v. United States*, 139 S. Ct. 2116, 2141-42 (2019) (Gorsuch, J., dissenting) (explaining interaction between major-question and nondelegation doctrines); *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 159 (2000) (discussing interaction between major-question doctrine and APA). The United States makes two arguments about why Congress should be deemed to have delegated the authority to impose the HIPF on States. This Court should reject both.

First, the United States asserts (at 18, 34) that Congress has special leeway to allow agencies to define "technical" terms. The United States does not explain what it means by "technical," and no such distinction can be found in either the text of the Constitution or the Supreme Court's nondelegation jurisprudence. Instead, as Appellant-States explained (at 29), vague delegations have been approved only where the "boundaries of [the executive] authority," *Gundy*, 139 S. Ct. at 2129, can be drawn from other provisions of the statute, common usage, or common law. For example, in *United States v. Grimaud*, 220 U.S. 506 (1911) (cited at U.S. Br. 35), the Supreme Court allowed Congress to delegate to the Secretary of Agriculture authority to define acceptable "use and occupancy" of forested areas. But it was not because "use" is a technical term. Rather, it was because Congress provided significant guidance regarding what uses would be permitted, what types of "depredation" were to be prevented, and whether the resulting regulations could impact settlement of the relevant land. *Id.* at 507, 509.

Whitman v. American Trucking Associations, 531 U.S. 457 (2001), is not to the contrary. The United States selectively quotes *Whitman* (at 34) to make it appear as if the Court distinguished between technical and non-technical terms. *Whitman* states instead that Congress need not provide "any direction to the EPA regarding the manner in which it is to define 'country elevators,'" a relatively narrow and inconsequential term. *Id.* at 475. By contrast, the Court explained, Congress does need to "provide substantial guidance on setting air standards that affect the entire national economy." *Id.* It is thus the importance of the question, not its technical nature that is determinative.[3]

Given the undeniable importance of the Medicaid program to both the federal and state governments, *Whitman* would require at least the level of detail seen in *Grimaud.* None exists. Indeed, as Appellant-States explained (at 6-9, 30), the Certification Rule was promulgated because even in 2002, actuaries could not agree on prescriptive standards to define "actuarial soundness" in the Medicaid-MCO context. As with many of the other arguments that Appellant-States made in their principal brief, the United States makes no substantive response. Under Rule 28, any such arguments should be deemed to be undisputed. *E.g.*, *United States v. Guillen-Cruz*, 853 F.3d 768, 777 (5th Cir. 2017) (citing *Hernandez v. Garcia Peña*, 820 F.3d 782, 786 n.3 (5th Cir. 2016)). It is hard to imagine a clearer example of an impermissible delegation than allowing an agency to define a term that experts could not define more than two decades after the passage of the statutory standard. Under the important-decision doctrine applicable in *Chevron* "Step 0," the Court should consider

[3] Equally meritless is the United States' assertion (at 16) that Appellant-States declined to defend the district court's ruling about the private nondelegation doctrine. Appellant-States were not obliged to follow or defend the United States' description of the district court's reasoning, which was inaccurate.

this constitutional difficulty in determining the scope of the Executive's discretion to impose the HIPF. *Brown & Williamson*, 529 U.S. at 159.

Second, the United States asserts (at 27-28) that the ACA's significance does not mandate application of the important-decision doctrine. Appellant-States never said it did. Rather, since the Founding, our system of government has given special significance to the decision to impose taxes. Indeed, that decision was considered so sensitive that the Founders required that all bills imposing a tax originate in the House as the governmental body most responsive to the will of the people. Priscilla H. M. Zotti & Nicholas M. Schmitz, *The Origination Clause: Meaning, Precedent and Theory from the 12th to the 21st Century*, 3 BRIT. J. AM. LEGAL STUD. 71, 91-98 (2014). Since then "[j]udicial attitudes towards delegations of power in the field of taxation have been particularly unfavorable." SINGER & SINGER, *supra*, § 4:22. Moreover, the imposition of a tax on sovereign States alters the balance between the federal and state government. Under such circumstances any ambiguity weighs against a delegation of authority—*particularly* in a closely negotiated piece of legislation like the ACA. *See Gregory v. Ashcroft*, 501 U.S. 452, 464 (1991) (citing LAURENCE TRIBE, AMERICAN CONSTITUTIONAL LAW § 6.25 (2d ed. 1988)). Because Congress did not clearly allow the Executive to impose the HIPF on States, this Court should hold that no such delegation occurred. *Nixon v. Mo. Mun. League*, 541 U.S. 125, 140-41 (2004).

2. *Chevron Step 1.* Far from providing a plain statement that the Executive could impose the HIPF on States, Congress said the opposite. For the reasons Appellant-States explained (at 16-18), the text, history, and purpose of Section 9010 of the

Patient Protection and Affordable Care Act, Public Law 111-148, 124 Stat. 120 (Mar. 23, 2010), all lead to one conclusion: that Congress intended to exempt States from paying the HIPF, including when they manage their Medicaid systems through an MCO model. The United States makes three responses. None has merit.

First, the United States reiterates (at 5-6) its assertion that Congress only exempted States when they operate their Medicaid programs in a fee-for-service model. The federal government does not dispute that this is inconsistent with the thirty-year push for States to adopt an MCO model. *Cf.* ROA.1611-12, 1860. Nevertheless, the United States asserts (at 8) that its view makes sense because when the ACA was being debated, at least two States were considering an entirely new healthcare model. The general rule in applying *Chevron* Step 1 is that a court must look to the law as it *exists* and "interpret the statute as a symmetrical and coherent regulatory scheme." *BNSF Ry. Co. v. United States*, 775 F.3d 743, 751 & n. 62 (5th Cir. 2015) (quoting *Brown & Williamson*, 529 U.S. at 133)). Appellant-States are aware of no principle that allows the Court to interpret federal law in light of yet-to-be-adopted state legislation.

At its core, the United States' argument depends on its assertion that because MCOs remit the HIPF assessed on state contracts to the IRS, they are the entities being taxed. Since the earliest days of the Republic, courts have refused to take such a formalistic view of tax legislation. *E.g.*, *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 396 (1819) ("The Bank of the United States is as much an instrument of the government for fiscal purposes, as the courts are its instruments for judicial purposes."). Instead, courts look to what entity bears the incidence of the tax—a question that turns not on who cuts a check to the relevant taxing authority, but on who bears the economic burden of the tax if it is paid or the legal consequences if it is not. *E.g.*, *North Dakota v. United States*, 495 U.S. 423, 435 (1990) (plurality op.). As Appellant-States explained (at 51-52), States bear 100% of the cost of the HIPF imposed on their contracts, and they are the only entities who will suffer legal consequences if the HIPF is not paid. The United States responds (at 6) that private insurers have no statutory exemption from the HIPF. That ignores, however, that the HIPF is calculated based on the insurers' market share. ACA § 9010(b). The United States acknowledges (at 41) that if a State does not pay the HIPF on an MCO contract, that contract will never go into effect. In that circumstance, even without an exemption, the MCO will not be responsible to pay the HIPF because the contract will never be taken into account in dividing the HIPF among participants in the health-insurance industry. ACA § 9010(b)(2). *Someone else* will simply have to pay a higher percentage of the overall assessment.

Because States bear the legal incidence of the HIPF when it is imposed on their MCO contracts, States are not trying to expand an exemption to third parties. *Contra* U.S. Br. 1. Instead, the ACA unambiguously exempts them from paying the HIPF, even if they pay the tax through the intermediation of a third party. ACA § 9010(c)(2)(B).

Second, the United States argues (at 9) that Appellant-States are advocating an "atextual" interpretation of Section 9010 based on the ACA's history and purpose. Properly understood, however, textualism looks for the "fair meaning of the law," in its larger statutory and regulatory context. ANTONIN SCALIA & BRYAN A. GARNER,

READING LAW: THE INTERPRETATION OF LEGAL TEXTS 355-56 (2012) (explaining the difference between textualism and strict constructionism). The Supreme Court has made abundantly clear that when evaluating statutory text under the first step of the *Chevron* analysis, courts must "apply[] the ordinary tools of statutory construction" to determine whether Congress spoke to a particular issue. *City of Arlington v. FCC*, 569 U.S. 290, 296 (2013). These "'traditional tools of statutory interpretation' includ[e] 'text, structure, purpose and legislative history.'" *BNSF Ry. Co.*, 775 F.3d at 751 (quoting *Citizens Coal Council v. Norton*, 330 F.3d 478, 481 (D.C. Cir. 2003)). Appellant-States obeyed this command when they discussed the text of Section 9010 and how it functions in its statutory context, pointing to purpose and legislative history only as further support of their interpretation of the statute's plain language.[4]

Third, the United States asserts (at 25) that Congress ratified the Certification Rule by referring to regulations relating to actuarial soundness in ACA § 2501. As amici have acknowledged, this supposed ratification addresses actuarial soundness in a "different context." Blue Cross Br. 16. Specifically, Section 2501 addresses a rebate program relating to prescription medications. Prescription medications are an

[4] The United States' criticism (at 9) of Appellant-States' discussion of the HIPF's purpose is particularly ill-founded. The federal government conspicuously does not dispute Appellant-States' assessment of the HIPF's purpose, only their reliance on a description from the popular press. As the Supreme Court has recognized, however, more traditional sources for assessing statutory purpose are unavailable because "Congress wrote key parts of the [ACA] behind closed doors." *King v. Burwell*, 135 S. Ct. 2480, 2492 (2015) (citing John Cannan, *A Legislative History of the Affordable Care Act: How Legislative Procedure Shapes Legislative History*, 105 L. LIBR. J. 131, 163 (2013)).

optional benefit under Medicaid, *see Fisher v. Oklahoma Health Care Auth.*, 335 F.3d 1175, 1178 (10th Cir. 2003), and are addressed in an entirely different part of the Code of Federal Regulations than the Certification Rule, *compare* 42 C.F.R. § 438.6, *with id.* § 447.509. As a result, Congress's purported ratification of the role of actuarial standards in one context tells us little about Congress's understanding of those regulations in another.

More fundamentally, this argument begs the question of *what* Congress supposedly ratified. As Appellant-States have explained—and the United States nowhere disputes—the only actuarial standard specific to Medicaid-MCO contracts in existence in 2010 was a non-binding 2005 practice note that addressed only *state* taxes. ROA.1864-65. No federal premium tax had ever existed, and Section 9010 exempts States on its face. ACA § 9010(c)(2)(B). Under ordinary rules of statutory construction, the specific governs the general. SCALIA & GARNER, *supra*, 183 & n.1. Thus, even if Congress ratified the Certification Rule as a general matter, that ratification was subject to the States' exemption under the HIPF. And because Congress has spoken to the question, "Article III courts need not—indeed *must* not—outsource their constitutionally assigned interpretive duty to Article II agencies." *Forrest Gen. Hosp. v. Azar*, 926 F.3d 221, 228 (5th Cir. 2019) (emphasis in original).

3. *Chevron Step 2*. For many of the same reasons, the United States' defense of its actions under *Chevron* Step 2 fails. Apart from Congress's supposed ratification of the Certification Rule, the United States' only response is to question "why Congress's creation of the provider fee should alter what is and is not actuarially sound."

U.S. Br. 29.[5] Appellant-States explained (at 43) several unique aspects of the HIPF, which could impact how an actuary might treat it (*e.g.*, the fact that unlike other expenses, it is not tax deductible). The United States' response-by-way-of-rhetorical-question does not point to any evidence that HHS considered these "important aspect[s] of the problem" or offered an "explanation for its decision" to use the Certification Rule to apply the HIPF to States notwithstanding the exemption in Section 9010. *Luminant Generation Co., L.L.C. v. EPA*, 675 F.3d 917, 925 (5th Cir. 2012). As a result, the Court should hold that the Certification Rule is substantively unlawful under the APA.

B. ASOP 49 cannot be applied as binding federal law absent notice and comment.

Because the United States adopted and applied ASOP 49 as binding federal law without notice and comment, it has also violated the procedural limitations imposed by the APA. The United States again makes three responses, none of which has merit.

First, the United States asserts (at 30) that ASOP 49 is not a substantive rule requiring notice and comment because it merely reflects an application of the Certification Rule, which no one disputes went through notice and comment in 2002. As Appellant-States explained (at 44)—and the United States again does not dispute—

[5] The United States invokes (at 28-29) the rule that an agency's actions are typically assessed based on the record before it when the rule was promulgated (here in 2002). But it does not actually dispute that statutory changes *can* render a previously acceptable rule arbitrary—only whether the ACA makes any change that does so.

before ASOP 49, actuaries had discretion in accounting for the HIPF in State Medicaid MCO contracts. ROA.1863-65 (providing nonbinding list of fourteen factors actuaries could consider); ROA.2592 (stating only that "[t]he potential effect[s] of the fee may be considered"). ASOP 49 removed any such discretion. *E.g.*, ROA.1683, 1694.[6] The agency issued guidance that ASOP would be applied prospectively. ROA.3243. As a result, ASOP 49 is a substantive rule of HHS, *Texas v. EEOC*, 933 F.3d 433, 442 (5th Cir. 2019) ("[A]ctions that retract an agency's discretion . . . are binding."), and invalid without notice and comment, *id.* at 443-44; *see also, e.g.*, *Shell Offshore, Inc. v. Babbitt*, 238 F.3d 622, 629 (5th Cir. 2001). That the Certification Rule is so vague that it requires substantive rules to give it content is a separate problem with the Certification Rule. *United States v. Picciotto*, 875 F.2d 345, 347-48 (D.C. Cir. 1989). But it does not render HHS's adoption of ASOP 49 compliant with the procedural requirements of the APA.

Second, the United States asserts (at 30-31) that ASOP 49 is not a rule because it was promulgated by the ASB rather than a federal agency. This Court has recognized, however, that the classification of an agency action for APA purposes does not depend on whether the actor had "authority to promulgate substantive rules."

[6] While ASOP 49 nominally leaves some discretion, the uncontroverted evidence in the record is that this discretion is illusory. Appellant-States Br. 44 (collecting citations). An agency cannot avoid the conclusion that its policies are binding rules by including boilerplate language retaining discretion. *Texas v. United States*, 809 F.3d 134, 173 & nn. 136-37 (5th Cir. 2015), *aff'd by an equally divided court*, 136 S. Ct. 2271 (2016) (per curiam) (quoting *inter alia Gen. Elec. Co. v. EPA*, 290 F.3d 377, 383 (D.C. Cir. 2002)).

EEOC, 933 F.3d at 451. That the United States allowed a private entity to take actions that must, by law, be executed by an agency simply means that it violated *both* the APA *and* the Constitution. *E.g.*, *Pittston Co. v. United States*, 368 F.3d 385, 395 (4th Cir. 2004).

Third, the United States argues (at 31) that Appellant-States' claim fails because they did not ask for a modification of the Certification Rule in light of ASOP 49. Leaving aside an agency's inherent obligation to stay within the scope of its delegation, *see Contreras-Bovanegra*, 678 F.3d at 818, this argument is circular. It assumes that the agency's adoption of ASOP 49 was not *already* a rule requiring notice and comment. It was, and because no notice and comment occurred, it was invalid.

II. The HIPF Is Unconstitutional as Applied to States Through the Actuarial-Soundness Requirement.

A. States cannot be forced to pay the HIPF as a condition on receiving Medicaid funding.

The HIPF itself is also invalid as it has been applied to States—namely, as an improper condition on their receipt of Medicaid funding. In its defense of the statute, the United States asks the Court to read the HIPF purely as a tax, divorced from its interaction with other provisions of the U.S. Code. The United States further asks the Court to parse Congress's constitutional powers in a way that is not supported by Supreme Court case law or first principles. The Court should decline those invitations, particularly as the United States effectively admits that the HIPF violated the Spending Clause.

1. The United States is wrong when it asserts (at 35-38) that this case does not implicate the limits on Congress's power to spend because the HIPF was passed under the power to tax. The United States acknowledges (at 35) that Appellant-States have brought an as-applied challenge to the HIPF. Moreover, it concedes (at 37) that the HIPF has been applied to States through the actuarial-soundness requirement, which is a condition on spending. Courts examine whether a provision is unconstitutional by looking to how it functions in the context of other laws and regulations. *E.g.*, *United States v. Windsor*, 570 U.S. 744, 755 (2013); *Agency for Int'l Dev. (USAID) v. All. for Open Soc'y Int'l, Inc.*, 570 U.S. 205, 217-19 (2013). The Court should thus examine the constitutionality of the HIPF as it has been applied to States—namely, as a condition on spending.[7]

2. The United States next asserts (at 37-38) that under *National Federation of Independent Business v. Sebelius (NFIB)*, 567 U.S. 519 (2012), the taxing and spending powers are subject to different standards because they are different enumerated powers. The premise of this argument is wrong. In *NFIB*, the Supreme Court reiterated a well-established principle that Congress's power to "tax and spend" allows "the Federal Government considerable influence even in areas where it cannot directly regulate" under the Commerce Clause. *Id.* at 537 (comparing Congressional authority under U.S. CONST. art. I, § 8, cls. 1 & 3). But the Supreme Court has always considered the "power to tax and spend" as a single, unitary grant of authority. *Id.* at

[7] For this reason, the United States' discussion (at 36) about whether the HIPF is a tax is immaterial to the issues on appeal and requires no response here.

623 (Ginsburg, J., concurring); *see also, e.g.*, *Flast v. Cohen*, 392 U.S. 83, 115 (1968) (Fortas, J., concurring); *United States v. Butler*, 297 U.S. 1, 64 (1936).

This Court should not hold that Congress's power to tax extends more broadly than its power to spend. Both powers appear in the same clause, which allows Congress "to lay and collect Taxes . . . to pay the Debts and provide for the . . . general welfare." U.S. CONST. art. I, § 8, cl. 1. Outside the context of the Sixteenth Amendment, which is not applicable, there is no textual basis to conclude that Congress's power to raise money is more extensive than its power to spend it. Indeed, the powers are flipsides of the same coin. Almost any spending program can be reformulated as a tax, and parsing Congress's power in the manner that the United States suggests would render the finely tuned limits in *South Dakota v. Dole*, 483 U.S. 203 (1987), nugatory.[8]

It would be particularly inappropriate to recognize new distinctions within Congress's taxing and spending power in this case because, as discussed below, the HIPF violates *both* aspects of Congress's power to tax and spend. *Cf. New York v. United States*, 505 U.S. 144, 176 (1992) ("A choice between two unconstitutionally coercive regulatory techniques is no choice at all."); *cf. USAID*, 570 U.S. at 214-15.

[8] There may be instances when Congress can tax *individuals* in ways that may exceed its powers to influence States under the Taxing and Spending Clause both due to the Sixteenth Amendment and the fact that individuals are not sovereigns, rendering the anticommandeering concerns that drive the Supreme Court's Spending Clause jurisprudence inapposite. But the Court need not reach that question here.

3. The United States' assertions (at 38-43) about why the Taxing and Spending Clause allows Congress to force States to pay the HIPF to receive Medicaid funding prove the opposite. Assuming that a spending program serves the general welfare (which is not at issue), Congress may impose conditions on that spending only if (1) States had clear notice of the condition, (2) the condition is reasonably related to the federal interest served by the program, (3) the condition complies with other provisions of the Constitution, and (4) the condition does not cross the line of coercion. *E.g.*, *Dole*, 483 U.S. at 207, 211. Why the HIPF violates Appellant-States' intergovernmental tax immunity is discussed below. The United States' response demonstrates why imposing the HIPF as a condition on Medicaid also violates the other three limits on Congress's spending power.

First, the United States asserts (at 42-43) that Appellant-States were on adequate notice of the HIPF because the actuarial-soundness requirement was of long standing. *NFIB* requires, however, that courts scrutinize the structure and effect of the *particular* condition and whether it was predictable when a State accepted federal funds. 567 U.S. at 583-85. States may have known that the actuarial-soundness requirement is a condition on Medicaid, but, as the United States does not dispute, the HIPF was an unprecedented federal tax. *E.g.*, ROA.2754. The United States points to nothing that demonstrates that States were on notice that paying this multi-million-dollar tax was a condition of receiving Medicaid matching funds.

Second, the United States admits that the HIPF is used for purposes unrelated to Medicaid as it existed when Appellant-States opted to participate in the program. Indeed, the United States asserts (at 43) that the Court should reject Appellant-

States' position that the HIPF would be used "to 'cover the costs of providing coverage' to persons who are not Medicaid eligible" because Congress is not limited in its use of the funds by the structure and statutory history of the ACA. To the contrary, the federal government says, the funds can be spent "to fund all governmental programs." *Id.* That makes the constitutional violation worse. In *NFIB*, the Supreme Court held that Congress may not condition the receipt of Medicaid funding for the populations specified in 1965 on States' agreement to fund healthcare for populations made eligible only in the ACA. 567 U.S. at 583-84. That ruling cannot be squared with the United States' apparent position that Congress may condition the receipt of Medicaid funding for populations specified in 1965 on the States' agreement to pay for everything from aircraft carriers to the interstate highway system.

Third, the United States asserts (at 40-42) that States are not being coerced because MCOs pay the HIPF, and cooperative federalism allows MCOs to pass "some" of that burden on to States. As Appellant-States have exhaustively demonstrated, they are not paying "some" of the HIPF assessed on their contracts. They are paying all of it. And forcing one sovereign to pay taxes to another is *not* a part of federalism—whether or not that tax is intermediated through an independent entity. *E.g.*, *M'Culloch*, 17 U.S. at 396. Indeed, the only support the United States cites for this proposition holds that Congress *cannot* force States to fund abortions. *Harris v. McRae*, 448 U.S. 297, 309 (1980).

Also unavailing is the United States' hyperbole (at 41) that adopting the States' view would make even "benign" conditions on Medicaid unconstitutional. Whether a condition is "so coercive as to pass the point at which 'pressure turns into compulsion'" depends on the condition. *Dole*, 483 U.S. at 211. And there is nothing remotely comparable between a condition that "each State designate 'a single State agency to administer' the State's Medicaid plan," U.S. Br. 41 (quoting 42 U.S.C. § 1396a(a)(5)), and one that requires the States to pay hundreds of millions of dollars in taxes to fund unspecified priorities that—according to the United States' representations to this Court—may have nothing to do with Medicaid. *NFIB*, 567 U.S. at 582, 584.

In sum, because States must pay the HIPF as a condition of receiving Medicaid funds, it is subject to the limitations on Congress's ability "to tax and spend." *Id.* at 623 (Ginsburg, J. concurring). The United States' own admissions demonstrate why the HIPF violates those standards as applied to the States through the actuarial-soundness requirement.

B. The HIPF Violates Appellant-States' Intergovernmental Tax Immunity.

The HIPF is also unconstitutional as applied to the States because it violates Appellant-States' intergovernmental tax immunity. Again, the United States does not contest that the record evidence shows that Appellant-States bear the incidence of the HIPF when it is assessed on their MCO contracts.[9] In light of this concession, the HIPF is unconstitutional if *either* (1) the tax discriminates against States, or

[9] The United States also conspicuously does not dispute that its positions on appeal are inconsistent with the district court's reasoning for rejecting Appellant-States' tax claims—namely, that Congress "exempt[ed] the states from paying" the HIPF. ROA.4023.

(2) interferes with State sovereignty and is not a traditional source of revenue. *Massachusetts v. United States*, 435 U.S. 444, 457-58 (1978) (discussing test from *New York v. United States*, 326 U.S. 572, 586-87 (1946)). The HIPF does both.

1. The United States is wrong that the HIPF is not a discriminatory tax under *South Carolina v. Baker*, 485 U.S. 505 (1988), and *Alabama v. King & Boozer*, 314 U.S. 1 (1941), because MCOs remit the HIPF and only incidentally pass the cost on to States through higher prices. To the contrary, *Boozer* instructs courts to determine the actual target of the tax by examining who bears the burden of the tax under the "terms of the contract" and who will be held legally "liable for the tax" if the contract falls through. 314 U.S. at 9. That approach was reaffirmed in the cases upon which Appellant-States relied in their brief, including *North Dakota v. United States*, 495 U.S. 423 (1990), which was decided two years after *Baker*.

In *Boozer*, the incidence fell on the government contractor who would still be liable for a sales tax if its contract with the federal government collapsed. 314 U.S. at 12-13. In this instance, the United States does not dispute that MCOs will not be liable for the HIPF if Medicaid refuses to approve a contract because the State refuses to pay the HIPF. But States will be liable for the consequences of losing Medicaid funds. Appellant-States Br. 52. As a result, States bear the incidence of the HIPF.

Because of that conclusion, the Supreme Court's case law requires "the entire regulatory system [to] be analyzed to determine whether [the HIPF] is discriminatory 'with regard' to the economic burdens that result.'" *North Dakota*, 495 U.S. at 435 (plurality op.) (quoting *Washington v. United States*, 460 U.S. 536, 544 (1983));

accord id. at 451-52 (Brennan, J., concurring in part and dissenting in part) (agreeing on appropriate standard but reaching different conclusion). As *Baker* recognizes, Congress cannot pass a tax that "applies exclusively to [a State] and [is] levied . . . directly on the [State's] treasury . . . even if Congress allowed [the State] to escape the tax by restructuring its state government." 485 U.S. at 516. For the reasons that Appellant-States discuss (at 53), the regulatory system that allows the HIPF to be imposed on States at penalty of losing billions in Medicaid funding is discriminatory. The United States does not rebut that argument, choosing to rely entirely on the false premise that States are not being taxed.

2. Even if the HIPF were not discriminatory against States, it would still violate Appellant-States' intergovernmental tax immunity, because it is not a traditional source of revenue and impinges upon Appellant-States' sovereign interests in enforcing their own healthcare laws. The United States again does not dispute that the unprecedented HIPF fails this test, only whether it remains a separate test post-*Baker*. *See* U.S. Br. 45. *Baker* did not explicitly overrule this second test from *Massachusetts* and *New York*, and the Court should not infer that it implicitly did so either. *Baker* did not implicate this test because it involved the elimination of a personal-income-tax deduction for interest paid on unregistered bonds. *Baker*, 485 U.S. at 508-09. Income tax may not have been available to Congress "from the beginning," *Massachusetts*, 435 U.S. at 458 (citation omitted), but the Constitution was amended to allow Congress to impose such a tax, U.S. CONST. amend. XVI. And, unlike providing healthcare to underprivileged citizens, issuing bonds is not a uniquely sovereign function. *Baker*, 485 U.S. at 510 (noting that same statute applied to non-registered bonds issued by private corporations).

Because the HIPF fails to meet either test established by the Supreme Court for when a broadly applicable tax may be imposed on States, it runs afoul of the Tenth Amendment and cannot be applied to Appellant-States.

III. In the Alternative, Appellant-States Should Be Allowed to Pursue a Statutory Refund.

Because the HIPF could not lawfully be applied to Appellant-States, they and their taxpayers are entitled to recover the money they were required to pay as a condition on receiving Medicaid funding. The district court acted within its discretion in ordering those funds returned under principles of equitable disgorgement. But if the Court disagrees, Appellant-States are entitled to seek that money through a statutory refund claim. The United States' entire argument to the contrary (at 46-47) is that MCOs are the statutory taxpayer because the MCOs remit the HIPF to the IRS.

Generally speaking, Appellant-States do not dispute that parties "may not challenge the tax liabilities of others." *United States v. Williams*, 514 U.S. 527, 539 (1995). But the fact that MCOs cut the check to pay the HIPF to the IRS does not make them the taxpayers for statutory purposes any more than constitutional ones. Instead, "the word 'taxpayer' means not only the person against whom a tax is assessed (here, [the MCOs]) but also the person who actually pays the tax (here, [the States])." *Rothkamm v. United States*, 802 F.3d 699, 705 (5th Cir. 2015); *Colo. Nat'l Bank of Denver v. Bedford*, 310 U.S. 41, 52 (1940).

The United States argues (at 47) that this principle is limited to circumstances in which the party seeking a refund paid a tax *for* the nominal taxpayer. Here, the United States asserts, the party seeking the refund paid the tax *to* the nominal taxpayer. This would, however, hardly be the first time that the IRS has used third parties to collect taxes on its behalf. *E.g.*, *Cohen v. United States*, 650 F.3d 717, 719 (D.C. Cir. 2011) (en banc). For that reason, courts prefer "substance over form" in interpreting the tax code and "common sense inquiries over [the type of] formalism" the federal government currently advocates. *Williams*, 514 U.S. at 535-36.

The Court should reject the United States' reading of "taxpayer." Medicaid MCOs have absolutely no incentive to seek a refund because they do not bear the economic burden of the HIPF, and they will face no legal consequences if the tax is not paid. Because States both pay the HIPF and face the only legal consequence if it is not paid—*i.e.*, loss of Medicaid funding and associated legal consequences—they are the taxpayers entitled to a refund for statutory purposes. *Compare Stahmann v. Vidal*, 305 U.S. 61, 65-66 (1938) (concluding overall structure of tax made cotton producers taxpayer even when assessed against ginners), *with Boozer*, 314 U.S. at 3-10 (concluding that contractor was taxpayer because liable even if government did not pay on contract).

IV. The District Court Should Have Awarded Appellant-States Interest.

Finally, the district court should have awarded Appellant-States interest. By statute, Appellant-States would have been allowed to seek interest had they been successful on their tax-refund claim. 26 U.S.C. § 6611. And, as Appellant-States explained (at 26 n.12), the same considerations that led the district court to order equitable disgorgement should have led it to an award of interest.

The United States responds only (at 24 n.3) that Appellant-States waived their request by discussing the matter in a footnote. Arguments are waived only if they "are insufficiently addressed in the body of the brief." *Bridas S.A.P.I.C. v. Gov't of Turkmenistan*, 345 F.3d 347, 356 n.7 (5th Cir. 2007). Appellant-States fully explained (at 23-26) why the district court properly awarded equitable disgorgement above the line. Their assertion that the same reasoning should have led to an award of interest was placed in a footnote to avoid confusion because, as Appellee only, Wisconsin could not join the argument as to interest. *See* Rule 28(j) Letter filed Jan. 29, 2020. The Court should not treat such an action as a waiver but should instead address the request on the merits. *Cf. Martinez v. Mukasey*, 519 F.3d 532, 546 (5th Cir. 2008) (exercising discretion to address purely legal argument that was arguably waived).

Conclusion

The judgment of the district court should be affirmed in part, reversed in part, and remanded for further proceedings.

Respectfully submitted.

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Certificate of Service

On March 20, 2020, this brief was served via CM/ECF on all registered counsel and transmitted to the Clerk of the Court. Counsel further certifies that: (1) any required privacy redactions have been made in compliance with Fifth Circuit Rule 25.2.13; (2) the electronic submission is an exact copy of the paper document in compliance with Fifth Circuit Rule 25.2.1; and (3) the document has been scanned with the most recent version of Symantec Endpoint Protection and is free of viruses.

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Certificate of Compliance

This brief complies with: (1) the type-volume limitation of Federal Rule of Appellate Procedure 28.1(e)(2)(C) because it contains 6,376 words, excluding the parts of the brief exempted by Rule 32(f); and (2) the typeface requirements of Rule 32(a)(5) and the type style requirements of Rule 32(a)(6) because it has been prepared in a proportionally spaced typeface (14-point Equity) using Microsoft Word (the same program used to calculate the word count).

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