Issue Brief

The Law Behind Health Reform

Understanding the Individual Mandate & Constitutional Authority

Pablo Cardona, J.D., Health Policy Program

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In March 2010, President Barack Obama signed The Patient Protection and Affordable Care Act, or ACA, into law. No component of the far-reaching law is more contentious than the requirement that all citizens obtain health insurance. The Obama Administration's view is that this minimum coverage provision is essential to the vast expansion of insurance coverage.

Under the new law, health insurance providers cannot deny coverage due to pre-existing conditions. The minimum coverage provision not only ensures that millions more Americans will be covered, it simultaneously prevents individuals from waiting to obtain coverage until they need it. With pre-existing conditions no longer a barrier to coverage, individuals who choose to go "coverage free" until they become sick drive up the costs for all those who maintain coverage. The "individual mandate" as it is commonly known, is consequently the lynchpin in the law. Without it, health insurance costs would increase.

Much of the controversy about the individual mandate revolves around whether it is constitutional. Congress must have the power to require that all citizens obtain health insurance, otherwise, the individual mandate will run afoul the Constitution. The authority for the individual mandate comes from two sections of the Constitution: (1) the Commerce Clause and (2) the General Welfare Clause.

Legal history on the aforementioned constitutional powers can be split into two eras: the *Lochner* Era and post-*Lochner* era. The *Lochner* era, between roughly 1890 and ending in 1937, represents a very conservative and free market approach to judicial decision-making.[1] In the landmark case *Lochner v. New York,*[2] the Supreme Court struck down a worker safety law limiting the hours a person could work in a bakery on the basis that the regulation interfered with an individual's right to contract. The Court continued to strike down regulations that interfered with an individual's economic due process rights under the 14th Amendment.[3] The era ended in 1937, with the case *West Coast Hotel v. Parrish,*[4] where the Court upheld the constitutionality of a minimum wage law.

This brief provides an explanation of the constitutional challenges to the individual mandate. It explores Congressional power under the Commerce Clause and General Welfare Clause and the legal history supporting each power. It also applies both powers to the Affordable Care Act and provides an analysis of the constitutional concerns within that context.

The Commerce Clause

Congress shall have power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes

U.S. Constitution, Section 8, Clause 3

Congress has wide deference in its use of the Commerce Clause. Since the early 1940s, the Courts adopted an expansive interpretation of the Commerce Clause, enabling Congress to reach into previously excluded personal and intrastate activities. The Supreme Court defined those areas of activities under Congressional regulation as (1) the channels of interstate commerce, (2) the instrumentalities of interstate commerce, and persons or things in interstate commerce, and (3) activities that substantially affect interstate commerce."[5]

The Supreme Court first expanded its interpretation of the Commerce Clause in the 1942 case of *Wickard v. Filburn*.[6] In *Wickard*, the Supreme Court determined whether pursuant to the Agricultural Adjustment Act, Congress could regulate the amount of wheat a Farmer grew, even if the wheat was for personal use and never introduced into commerce. The Court upheld the regulation, finding that because of the impact Farmer Filburn's surplus had, in the aggregate, on the interstate wheat market, it was a valid exercise of the Commerce power. The Court stated, "The power to regulate commerce includes the power to regulate the prices at which commodities in that commerce are dealt in and practices affecting such prices."[7] Pursuant to *Wickard*, Congress had the power to determine whether wheat, not introduced into interstate commerce, affected the interstate market, thus obstructing the purpose of the Agricultural Adjustment Act.

The Court reaffirmed the expansion of federal power under the Commerce Clause in *Gonzales v. Raich*,[8] deciding whether the federal government had the power to prohibit the growth and personal possession of marijuana in compliance with California law. Writing for the majority, Justice Stevens cited *Wickard* extensively and argued that "Congress can regulate purely intrastate activity that is not itself commercial . . . if it concludes that failure to regulate that class of activity would undercut the regulation of the interstate market in that commodity."[9] The Court reasserted that federal regulation included private intrastate activities that had no direct impact on the interstate market.

Both *Gonzales* and *Wickard* demonstrate the federal government's power to regulate activities that are personal and intrastate, rather than explicit channels or instrumentalities of interstate commerce. However, although Congressional power under the Commerce Clause is seemingly plenary, the power is constrained to regulate only those activities that are economic in nature. This distinction was articulated under the Rehnquist Court in *United States v. Lopez*.[10] In *Lopez*, the Court determined that the Gun-Free School Zones Act of 1990 was a criminal statute and "had nothing to do with commerce or any sort of economic enterprise." The Court explained the distinction again in *United States v. Morrison*[11] where they found the Violence Against Women Act of 1994 unconstitutional, stating that "gender-motivated crimes of violence are not, in any sense of the phrase, economic activity . . . [T]hus far in our Nation's history our cases have upheld Commerce Clause regulation of intrastate activity only where that activity is economic in nature."[12] The Court found that both the Gun-Free School Zones Act and the Violence Against Women Act, were neither economic in nature, nor substantially affected interstate commerce, thus failing all three of Justice Steven's defined activities in *Raich*.

The language in the Affordable Care Act directly states that health care insurance and health care services are interstate economic activity. The new health care law is a mandate on an individual level and under the new law the commercial activity regulated is expressly described as an interstate economic activity. Section 1501(a)(2) of the bill is entitled, "Effects on the National Economy and Interstate Commerce" and follows with a detailed list of such effects.[13] Further, according to the Democratic Policy Committee,

"spending on health care has a substantial effect on interstate commerce because individuals buy and use health insurance across state borders, national health spending is projected to make up almost 18 percent of our nation's economy and the costs of providing emergency medical services to the uninsured has a significant impact on health care costs."[14]

Accordingly, the Obama Administration argued that, similar to *Wickard*, under the Commerce Clause, Congress has the ability to regulate private activities that would affect the health insurance market. If individuals choose to opt out of the market, premiums for individuals in the market would skyrocket. The Administration further argued that everybody, even the healthiest person, is a member of the health care market.[15] Fewer people covered by health insurance means a higher cost for everybody.

Opponents of this argument however distinguished *Wickard* from the individual mandates, suggesting that under the new law Congress is controlling an inactivity, not an activity. In an amicus brief filed with the Commonwealth of Virginia's lawsuit against the individual mandate, Georgetown Professor Randy Barnett argues the government has never before "said that every man, woman, and child faces a civil penalty for declining to participate in the marketplace . . . Even in . . . *Wickard v. Filburn* the federal government did not claim the power to mandate that people become farmers or enter into commercial transactions."[16] Congress, according to this argument, may have expansive power under the Commerce Clause, but that power does not extend to regulating inactivity.

In determining the constitutionality of the individual mandate pursuant to the Commerce Clause, a judge will have to determine (1) whether all individuals are members of the health insurance market and (2) whether an individual's decision not to purchase health insurance substantially affects interstate commerce. If the Court decides these issues favorably to the Administration, the regulation of the health insurance will be pursuant to the Commerce Clause and the application of the individual mandate will be pursuant to the Necessary and Proper Clause.[17]

The General Welfare Clause

The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States

U.S. Constitution, Section 8, Clause 1

In 1936, the Supreme Court struck down President Franklin Roosevelt's Agricultural Adjustment Act (AAA) in the case *United States v. Butler*,[18] dealing a blow to New Deal agricultural policy. The Court argued that Congress cannot use its taxing and spending powers to "purchase compliance" from farmers for a regulatory purpose, where that regulation was the sole jurisdiction of the states.[19] In *Butler*, the Court established the precedent that Congress has a substantive power to tax and appropriate for the general welfare—i.e. Congress can raise and spend public money for purposes that are not enumerated in the Constitution, if that purpose is for the general welfare. Although the Court took an expansive view of the General Welfare Clause, the predominant and coercive regulatory effect in *Butler* removed the Act from Congress's constitutional authority. Relying on the *Child Labor Tax Case*,[20] the Court decided that the AAA was an improper exercise of the federal taxing power since it was designed as a statutory plan to regulate and control agricultural production—an area reserved to the States.

United States v. Butler was decided in the final years of the *Lochner* era, a period of judicial history where federal regulation was severely constrained. Following the 1937 decision of *West Coast Hotel v. Parrish*, however, the Court shifted to a progressive view of economic regulation and FDR's New Deal moved forward. The Court's decisions in *Steward Machine Co. v. Davis*[21] and *Wickard v. Filburn* looked favorably upon *Butler's* expansive view of the general welfare clause, however, unlike *Butler* did not find

the Act coercive or beyond the powers of the federal government. Under *Wickard*, the Supreme Court upheld a new Agricultural Adjustment Act of 1938 pursuant to the Commerce Clause.

In the spring of 2010, the White House's legal team changed course and argued that the individual mandate was constitutional, pursuant to the General Welfare Clause. Though at the time most legal scholars agree that the Commerce Clause was a sufficient source of power for the mandate, the taxing power introduced new challenges on both sides. Congressional power "to lay and collect taxes . . . for the general welfare" under Article 1 section 8 is considered "plenary," meaning general. Congress can tax and spend for numerous reasons with few limitations. The Court's have found that if a tax infringes on a 'fundamental right' it is subjected to a higher level of scrutiny. Additionally, if a tax is designed as coercive and strictly for a regulatory purpose rather than raising revenue, the Court's have similarly struck it down.

This revenue-raising limitation has become a fine line in Constitutional interpretation and is an area of contention in the challenges to the new health care law. The 1937 ruling in *Sonzinsky v. United States* stated that a federal tax could be valid even though it has a regulatory effect.[22] However, even though a tax can have a regulatory effect it must be a valid tax—it must raise revenue for the general welfare.

In *Commonwealth of Virginia v. Sebelius*, the administration's lawyers maintain that the Minimum Essential Coverage Provision (sec. 5000A) is a genuine revenue-raising device that is directly related to "the goal of requiring every individual to pay for the medical services they receive." However, in its lawsuit, Virginia argues that the tax (referred to as a "penalty" in sec. 5000A) is intended not to generate revenue but to regulate conduct. Since it would generate little if any revenue and is a penalty rather than a tax, Virginia argues, Congressional authority must be from an enumerated power—otherwise, the provision interferes with an area of regulation reserved to the states.

Conclusion

The essential fight over the Minimum Essential Coverage Provision largely depends on the resolution of two crucial decisions: (1) whether the "penalty" can stand alone as a genuine tax, and (2) if not, whether Congress has the authority under the Commerce Clause to regulate economic inactivity through a tax.

The government has a much tougher challenge in arguing that the penalty is a tax. In addition to President Obama's repeated statements that the penalty is not a tax the deliberate use of the word "penalty" in sec. 5000A rather than "tax" (tax is used in other areas of the law to mean tax) gives the Commonwealth's argument more credibility.

The Administration, however, has the law on its side. It is unlikely that the Court will diverge from the expansive view of federal power held since the late 1930s. Although, the individual mandate raises a unique question regarding inactivities and revenue-raising taxes/penalties, the real issue of Constitutional authority is whether health care is a class of activity of which all citizens are members. If it is, then the government has the constitutional power to require health insurance of all citizens.

Notes

1 Available at http://topics.law.cornell.edu/wex/lochner_era.

2 198 U.S. 45 (1905)

3 *See*, Hammer v. Dagenhurt 247 U.S. 251, (1918) (Supreme Court struck down Child Labor law illustrating a distinction between the manufacturers of interstate commerce and the goods of interstate commerce.) *See also*, Bailey v. Drexel Furniture Co., 259 U.S. 20 (1922) (Supreme Court found Child Labor Tax Law unconstitutional since its purpose was as a penalty and not a tax.)

4 300 U.S. 379 (1937)

5 *Gonzales v. Raich*, 545 U.S. 1, 16-17 (2005).

6 317 U.S. 111 (1942)

7 317 U.S. at 128

8 545 U.S. 1 (2005)

9 *Id.* at 3.

10 514 U.S. 549 (1995)

11 529 U.S. 598 (2000)

12 *Id.* at 613.

13 (A) The requirement regulates activity that is commercial and economic in nature: economic and financial decisions about how and when health care is paid for, and when health insurance is purchased. (B) Health insurance and health care services are a significant part of the national economy. National health spending is projected to increase from $2,500,000,000,000, or 17.6 percent of the economy, in 2009 to $4,700,000,000,000 in 2019. Private health insurance spending is projected to be $854,000,000,000 in 2009, and pays for medical supplies, drugs, and equipment that are shipped in interstate commerce. Since most health insurance is sold by national or regional health insurance companies, health insurance is sold in interstate commerce and claims payments flow through interstate commerce. (C) The requirement, together with the other provisions of this Act, will add millions of new consumers to the health insurance market, increasing the supply of, and demand for, health care services. According to the Congressional

Budget Office, the requirement will increase the number and share of Americans who are insured. (D) The requirement achieves near-universal coverage by building upon and strengthening the private employer based health insurance system, which covers 176,000,000 Americans nationwide. In Massachusetts, a similar requirement has strengthened private employer-based coverage: despite the economic downturn, the number of workers offered employer-based coverage has actually increased. (E) Half of all personal bankruptcies are caused in part by medical expenses. By significantly increasing health insurance coverage, the requirement, together with the other provisions of this Act, will improve financial security for families. (F) Under the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1001 et seq.), the Public Health Service Act (42 U.S.C. 201 et seq.), and this Act, the Federal Government has a significant role in regulating health insurance which is in interstate commerce. (G) Under sections 2704 and 2705 of the Public Health Service Act (as added by section 1201 of this Act), if there were no requirement, many individuals would wait to purchase health insurance until they needed care. By significantly increasing health insurance coverage, the requirement, together with the other provisions of this Act, will minimize this adverse selection and broaden the health insurance risk pool to include healthy individuals, which will lower health insurance premiums. The requirement is essential to creating effective health insurance markets in which improved health insurance products that are guaranteed issue and do not exclude coverage of preexisting conditions can be sold. (H) Administrative costs for private health insurance, which were $90,000,000,000 in 2006, are 26 to 30 percent of premiums in the current individual and small group H. R. 3590—126 markets. By significantly increasing health insurance coverage and the size of purchasing

pools, which will increase economies of scale, the requirement, together with the other provisions of this Act, will significantly reduce administrative costs and lower health insurance premiums. The requirement is essential to creating effective health insurance markets that do not require underwriting and eliminate its associated administrative costs.

14 The Democratic Policy Committee, at http://dpc.senate.gov/docs/fs-111-2-49.html.

15 Melissa Nelson, "Lawsuit on Obama health plan likely going to trial," The Washington Post, Sept. 12, 2010. Available at http://www.washingtonpost.com/wp-dyn/content/article/2010/09/14/AR2010091400990.html.

16 Available at http://www.cato.org/pubs/legalbriefs/VA_v_Sebelius.pdf.

17 "The Congress shall have Power - To make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof." Article 1, sec. 8, cl 18.

18 297 U.S. 1 (1936)

19 *Id.* at 74.

20 *Bailey v. Drexel Furniture Co.*, 259 U.S. 20 (1922)

21 301 U.S. 548 (1937) (Arguing that a tax is not unconstitutional simply because it has a regulatory effect.) *See also*, Sonzinsky v. United States, 300 U.S. 506 (1937).

22 300 U.S. 506, 513 (1937) ("Every tax is in some measure regulatory. To some extent it interposes an economic impediment to the activity taxed as compared with others not taxed. But a tax is not any the less a tax because it has a regulatory effect . . . and it has long been established that an Act of Congress which on its face purports to be an exercise of the taxing power is not any the less so because the tax is burdensome or tends to restrict or suppress the thing taxed" (internal citations omitted)(emphasis added)).

MAIN OFFICE
1899 L Street, NW
Suite 400
Washington, DC 20036
Phone 202 986 2700
Fax 202 986 3696

CALIFORNIA OFFICE
921 11th Street
Suite 901
Sacramento, CA 95814
Phone 916 448 5189

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