July 1, 2013


CC:PA:LPD:PR (REG-106796-12)
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

RE: The $500,000 Deduction Limitation for Remuneration Provided by Certain Health Insurance Providers

To Whom It May Concern:

The U.S. Chamber of Commerce (the “Chamber”) submits these comments in response to the Proposed Rule on the $500,000 deduction limitation for remuneration provided by certain health insurance providers, (“Proposed Rule”), published in the Federal Register on April 2, 2013 and issued by the Department of Treasury (“Treasury”) and the Internal Revenue Service (“IRS”).

The Proposed Rule implements an amendment to the Internal Revenue Code that limits the allowable deduction for remuneration attributable to services provided by applicable individuals to certain health insurance providers that receive premiums from providing health insurance coverage as imposed by section 9014 of the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation ACT of 2010, (“PPACA”).

The US Chamber of Commerce is the world’s largest business federation representing the interests of more than three million companies of every size, sector and region. The Chamber is a supporter of strong corporate governance policies that are a fundamental cornerstone for business practices and capital formation needed for economic growth and job creation in all sectors of the economy. Accordingly, the Chamber welcomes the opportunity to comment upon the Proposed Rule.


The Chamber has serious concerns that the caps on compensation deductibility, as required under the PPACA will have an adverse impact upon the operation and competitive position of health insurance providers.

**General Concerns Regarding Executive Compensation**

In 2009, the Chamber released a set of principles on corporate governance and executive compensation. These principles state in part:

- Corporate governance policies must promote long-term shareholder value and profitability but should not constrain reasonable risk-taking and innovation.

- Long-term strategic planning should be the foundation of managerial decision-making.

- Corporate executives’ compensation should be premised on a balance of individual accomplishment, corporate performance, adherence to risk management and compliance with laws and regulations, with a focus on shareholder value.

- Management needs to be robust and transparent in communicating with shareholders.³

We believe that these principles should still guide policymakers as they consider corporate governance and executive governance rules for companies to follow in a 21st century global economy.

Section 9014 creates a cap upon the deductibility of remuneration paid by certain health insurance providers at $500,000. We believe that this cap places health insurance providers at a competitive disadvantage.

First, the section 9014 cap places health insurance providers on a different level than every other public company in the United States who can deduct up to $1 million in executive compensation. While compensation deductibility caps for public companies only apply to the Chief Executive Officer and the top four executives, section 9014 is much broader for two reasons: (1) section 9014 encompasses all officers, directors and employees for health insurance providers; and (2) it removes all the performance-based exceptions provided for under Section 162(m) for health insurance providers. It should be noted that companies must compete for talent and a means of doing so is through compensation packages. By placing health care insurance providers at a lower threshold and a wider net than other public companies, it will become more expensive and difficult for insurers to compete for talent.

---

³ Letter from U.S. Chamber of Commerce to Treasury Secretary Timothy Geithner, February 6, 2009.
Secondly, compensation deduction caps have not achieved their intended purpose and have led to other forms of compensation at higher levels. In 1993, the Clinton Administration placed the $1 million dollar cap on deductibility for executive compensation in a bid to drive compensation below the $1 million dollar level. Instead, compensation rose by over 250% in part because compensation began to take other forms, directly contributing to the rise of stock options.

Therefore, the deductibility cap did not achieve its intended purpose and in fact may make it more difficult for health insurance providers to operate in an environment that is increasingly competitive for both resources and talent. By placing this cap on compensation, history shows that unintended consequences may occur with compensation throughout the health insurance industry, contrary to the intent of the provision. Those unintended consequences may also lead to negatively impair the ability of those firms to deliver health insurance to the American public as a result.

**Specific Concerns with Regard to Corporate Transactions**

*Attribution of Compensation to Taxable Years*

While we appreciate the ability to use the time period from the grant date to the exercise date to attribute the compensation to the taxable years, we understand that some service providers are concerned that utilizing the grant to exercise period would create additional complexities in the recordkeeping and may be cost prohibitive. Therefore, we would like to have the flexibility of opting to use either the methodology of grant date to exercise date as proposed in the regulations or the option to use the methodology employed by the CHIP for Generally Accepted Accounting Principles (“GAAP”) or Statutory Accounting Principles (“SAP”). This would give the options of attributing the income over the grant to vesting date. Using the grant to vesting period could: reduce the number of years that the compensation is spread; reduce the complexity of the recordkeeping; and generally increase the amount of the limitation. This reduced complexity, could also reduce the amount of consulting expenses that will need to be incurred with concerned service providers.

*Aggregated Group*

The PPACA and Proposed Rule apply the section 162(m)(6) deduction limits to a covered health insurance provider (“CHIP”) and to any entity that is part of an aggregated group that includes a CHIP. We believe however, if any corporation that is not a post-2012 CHIP leaves an aggregated CHIP group, that corporation is no longer subject to the deduction limits, even with respect to employees that are continuing to receive compensation for services performed during the period the corporation was part of the aggregated group.

In this regard, Proposed Rule section 1.162-31(f)(1)(i) states in part that –

… if a member of an aggregated group purchases a health insurance issuer that is a [CHIP] (so that the health insurance issuer becomes a member of the aggregated group), each member of the acquiring aggregated group
generally will be a [CHIP] for the taxable year in which the corporate transaction occurs and each subsequent taxable year in which the health insurance issuer continues to be a member of the group…. [Emphasis added.] 4

The implication of the emphasized language is that a corporation that is not a CHIP in an aggregated group that includes a CHIP would no longer be subject to 162(m)(6) when a corporate transaction occurs which causes the corporation to not be part of the aggregated group. We request that the Final Rules clarify this treatment, such as through inclusion of an example in the Final Rules.

ARBITRARY AND UNSUBSTANTIATED OMISSION ECONOMIC ANALYSIS

In the Proposed Rule, the Treasury and IRS state that “It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined by Executive Order 12866 [and] therefore, a regulatory assessment is not required.”5 However, the omission of any substantive discussion of the potential costs and benefits of the proposed rule is a flagrant violation of both the letter and the spirit of Executive Order 12688 and of President Obama’s more recent Executive Order 13563.

The assertion that “it has been determined” that the Proposed Rule is not a significant rulemaking is arbitrary: no reasoning, data, calculations, evidence or facts are presented to support that conclusion. The statement is, additionally, obfuscatory, because it is not stated “who” has made this arbitrary determination.

Under Executive Order 12866, there are four possible reasons for a rule to be designated as a significant regulatory action. See E.O. 12866, Section 3 (f):

(f) “Significant regulatory action” means any regulatory action that is likely to result in a rule that may:
(1) Have an annual effect on the economy of $100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities;
(2) Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency;
(3) Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or
(4) Raise novel legal or policy issues arising out of legal mandates, the President’s priorities, or the principles set forth in this Executive order.

Treasury and the IRS are obligated to consider whether or not the Proposed Rule is significant under the terms of each of the four possible significance triggers and to

5 (78, Federal Register 63 at page 19960, “Special Analyses”)
explain in the preamble the reasons for its conclusions in each instance. With respect to (f)(1), economic significance, Treasury and the IRS should demonstrate by monetary calculations its estimate of the annual economic cost of the proposed rulemaking to show whether or not its estimated cost is below the $100 million annual trigger.

**Economic Impact Is In Fact Significant**

In particular, Treasury and the IRS should include in their analysis and calculations of economic cost consideration of the probable effect of the $500,000 limitation of expense deductions on the prices (premiums charged) for health insurance coverage. The limitation has the effect of increasing taxes paid by affected insurers. To the extent that previously deductible expenses will no longer be deductible, it is reasonable to consider that some or all of the cost impact of increased tax liability on affected insurers will be passed to health insurance consumers (individuals or employers providing group coverage contributions). To the extent that the increased tax liability cost is not passed to consumers, it may result in reduced dividends (or equity) to shareholders, reduced compensation of targeted employees, or reductions in operational investment (which could adversely impact the quality of services provided to the health insurance market.

An insurer may also avoid increased tax liability by reducing compensation of targeted employees to the deduction threshold, but that response also has potentially adverse economic impacts on the quality and efficiency of the health insurance market and indirectly on the quality and cost of health care. For example, reduction in compensation of certain skilled employees in the health insurance industry compared to their opportunities in other industries may result in a drain of talent from the health insurance industry and a concomitant reduction in efficiency, productivity and innovation.

In addition to the direct cost of the Proposed Rule (and the underlying statute) to increase tax liabilities of insurers or to reduce compensation of targeted employees, the Proposed Rule will also impose significant additional administrative costs on affected insurers. These costs include the direct labor costs of monitoring, reviewing and calculating compensation levels to determine the incidence of cases where the deduction limit applies. The costs of preparing tax returns and of preparing and maintaining supporting documentation will also increase. Many potentially affected insurers may also incur additional costs for the services of external legal counsel, accountants and consultants to ensure their accurate compliance with the proposed rule. These are all costs that the Treasury and IRS failed to consider, calculate and reveal in its rulemaking proposal.

President Obama’s Executive Order 13563 explicitly directs agencies to examine and monetarily estimate the income transfer effects of proposed regulations in addition to the cost and benefit effects specified in Executive Order 12866. The economic impacts described above (price increases to consumers, reduced compensation of employees, and reduced dividends or equity to shareholders) may have the effect of income or wealth transfers, as well as having cost effects. The Treasury and IRS have failed in their duty to analyze this aspect as required by the Executive Order. Furthermore, the Treasury and IRS should be aware that Executive Order 12866 defines an economically significant
regulation as one having an annual economic impact of $100 million or more and that
transfers as well as costs may comprise elements of the total economic impact.

**Cost-Benefit Analysis of Regulatory Alternatives Required**

Even if the Treasury and IRS were to find that the expected annual economic impact of
the proposed regulation is less than $100 million annually, they are still under
obligation by Executive Orders 12866 and 13563 to conduct and consider an analysis of
economic impacts of its selected regulatory approach and of alternative approaches. The
$100 million threshold only applies to the requirement to submit its analysis to
OMB/OIRA for review. Indeed, some analysis of cost and transfer impacts is logically
required to reasonably establish whether or not the threshold for OMB/OIRA review is
reached.

Even if a regulation is not deemed to be significant (economically or otherwise), agencies
are required by the Executive Order to identify, assess and consider the costs and benefits
of the various regulatory alternatives (not just the one specification chosen) and to choose
the approach that yields the greatest net benefit, unless the statutory authority requires
otherwise. The Executive Order does not provide any exception to this requirement.

The Executive Order encourages agencies to quantify the costs and benefits of the
selected regulatory approach and of alternatives considered to the extent feasible, but
permits qualitative assessment in cases where quantification is not possible. Neither
difficulty of measurement nor expectation of smallness of cost exempts the promulgating
agency from these responsibilities under the Executive Order. To be clear, even if the
costs of a regulation (and of each of its alternative formulations) is relatively small, this
would not justify ignoring the economic considerations.

Indeed, a rule with small costs may well also have small social benefits, and failure to
consider costs and benefits and to choose an approach randomly or arbitrarily would
carry a real risk that costs would exceed benefits. Given the thousands of regulatory
decisions made each year by Federal agencies, even small inefficiencies in regulatory
design are important and can add up to big inefficiencies and economic losses of output,
productivity and income.

The Treasury and IRS should also be aware that they cannot evade their duty to conduct
an analysis of the economic impact of the Proposed Rule by the appeal that they have
exercised no discretion in their rulemaking proposal. Even economic impacts of a
regulation that result from the underlying statute are legitimate impacts of the rulemaking
to implement the statute. Regulatory impacts are not limited to the impacts resulting
from the exercise of agency discretion. To claim otherwise would make the regulatory
impact assessment process both infeasible and un-useful. An important purpose of the
economic impact analysis required by Executive Orders (and also by the Regulatory
Flexibility Act, the Unfunded Mandates Act, and the Paperwork Reduction Act) are to
inform the President, the Congress and the public as to the full costs and benefits of
government mandates, including the costs of the statutory requirements that underlie the
implementing rules. In the case of this Proposed Rule, Congress may particularly benefit from information that informs it of the findings of a full and objective analysis of the economic costs and income/wealth transfer impacts of the statutory requirement that the regulation is designed to implement.

The intent of the Executive Orders is that agencies will approach the rulemaking task analytically and consider costs and benefits as an integral part of the regulatory decision-making process and not as an afterthought to justify a decision made arbitrarily. The Treasury and IRS admission that no economic analysis or impact assessment of the Proposed Rule has been done renders this proposed regulation unreasoned and arbitrary. The Treasury and IRS have acted in violation of the direct orders of the President of the United States. The Proposed Rule should be withdrawn, revised and resubmitted to include economic impact analysis that demonstrates compliance with Executive Orders 12866 and 13563.

CONCLUSION

While we recognize that the section 9014 caps were mandated by Congress, we hope you keep these views in mind as you contemplate the Final Rule. We believe that the Proposed Rule should be tailored in such a way as to minimize the impacts upon health insurance providers and avoid competitive disadvantages and unintended consequences. First, we recommend the Treasury and IRS permit flexibility so that CHIPs may use the methodology employed either for Generally Accepted Accounting Principles ("GAAP") or Statutory Accounting Principles ("SAP") audited financial statements. The Chamber also requests that Treasury and IRS clarify in the Final Rule that section 162(m)(6) will no longer apply to a corporation that is not a CHIP after it is no longer part of an aggregate group that includes a CHIP, even with respect to employees who are continuing to receive compensation for services performed during the period the corporation was part of the aggregated group. However, before a final rule is issued, we urge that the Treasury and IRS provide appropriate economic analysis regarding alternative regulatory approaches and of the likely economic impact of the approach taken in order to fulfill their obligations under the Executive Orders 12866 and 13563. We stand ready to meet with you to discuss these concerns further.

Sincerely,

Bruce Josten
Executive Vice President
Government Affairs