

# Legislative Brief

## Health Care Reform - Exchange Subsidies

July 25, 2014

### Contradictory Court Rulings on Federal Exchange Subsidies

#### Quick Facts:

- On July 22, 2014, two federal appeals courts issued inconsistent rulings on subsidies in states with federally-facilitated exchanges (FfEs)
- The U.S. Supreme Court may ultimately decide whether subsidies are available in all states, including those with FfEs.
- This issue may have a significant impact on employers due to ACA's employer mandate.

Several lawsuits have been filed by individuals and employers to challenge the ability of the federal government to provide tax credits under the Affordable Care Act (ACA) to individuals in states that did not establish their own Exchanges (that is, in states with federally-facilitated exchanges or FfEs). These lawsuits were filed in response to an Internal Revenue Service (IRS) [rule](#) that authorizes subsidies in all states, including those with FfEs.

#### Court Decisions

On July 22, 2014, two federal appeals courts—the District of Columbia Circuit Court and the 4th U.S. Circuit Court—issued inconsistent rulings on the availability of subsidies in states with FfEs. The lawsuits in *Halbig v. Burwell* and *King v. Burwell* were filed by individuals and employers in states that have FfEs. They argued that the IRS rule authorizing subsidies in all states conflicts with the text of ACA. They assert that, according to the law's plain language, ACA only authorized subsidies to be provided in states that have established their own Exchanges.

- In [Halbig v. Burwell](#), the D.C. Circuit Court held that the **IRS rule authorizing subsidies in states with FfEs is invalid**. In a 2-1 opinion, the court ruled that the IRS rule authorizing premium tax credits on FfEs violates clear statutory language since the text of ACA clearly states that subsidies are restricted to individuals in states that established their own Exchanges.
- In [King v. Burwell](#), the 4th Circuit Court unanimously **upheld the availability of the ACA's subsidies in states with their own Exchanges and in states with FfEs**. The statutory language—while arguably clear when considered in isolation—becomes ambiguous in light of the statute's goals, structure and related provisions (e.g., like that both the state and Federal Exchanges must report to the IRS about tax credits they provide). The [King](#) Court upheld the authority of the IRS to resolve this ambiguity in favor of providing tax credits in all Exchanges.

The Obama administration disagrees with the D.C. Circuit Court's ruling and intends to seek further review of the decision. It is anticipated that the Justice Department will ask the entire 11-person D.C. appeals court to review the decision. In the meantime, a Justice Department spokesperson has stated that the **subsidies will continue to remain available**.

#### Health Insurance Subsidies

ACA created health insurance subsidies to help eligible individuals and families purchase health insurance through an Exchange. The subsidies are designed to make coverage through an Exchange more affordable by reducing taxpayers' out-of-pocket premium costs. There are two federal health insurance subsidies available with respect to coverage through an Exchange: (i) premium tax credits and (ii) cost-sharing reductions. Both of these subsidies vary in amount based on the taxpayer's household income, and they reduce the out-of-pocket costs of health insurance for the insured.

- Premium tax credits are available for people with somewhat higher incomes (up to 400 percent of the federal poverty level (FPL)), and reduce out-of-pocket premium costs for the taxpayer.

- Reduced cost-sharing is available for individuals with lower incomes (up to 250 percent of the FPL). Through cost-sharing reductions, these individuals will be eligible to enroll in plans with higher actuarial values and have the plan, on average, pay a greater share of covered benefits. This means that coverage for these individuals will have lower out-of-pocket costs at the point of service (for example, lower deductibles and copayments).

### Health Insurance Exchanges

Effective for 2014, ACA requires each state to have an Exchange for individuals and small businesses to purchase private health insurance. According to the Department of Health and Human Services (HHS), the Exchanges allow for direct comparisons of private health insurance options on the basis of price, quality and other factors, and they coordinate eligibility for subsidies and other insurance affordability programs.

ACA delegated primary responsibility for establishing the Exchanges to individual states. However, because the U.S. Congress cannot require states to implement federal laws, ACA provides that HHS will operate the FFE in any state that refuses or is unable to set up an Exchange. For 2014, only 16 states and the District of Columbia established their own Exchanges. HHS operates the FFEs in the remaining 34 states (in some cases with state assistance, but in most cases not). Of the approximately 8 million people who selected private health plans from October through mid-April, over 5 million obtained coverage through an FFE. In addition, more than 4.5 million people have been determined eligible for subsidized insurance in the FFE.

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### Impact on Employers

For now, the IRS rule remains in effect and the administration has announced that federal subsidies will continue to be available to eligible individuals in all states, including those with FFEs. What this means:

- Premium tax credit subsidies and cost-sharing assistance in both the state and federally facilitated exchanges will continue to be distributed for the time being, and likely will be continually distributed until a final decision is made in the Burwell case or a similar case by the U.S. Supreme Court. Current individuals with subsidized coverage are unaffected by the ruling.
- If the Supreme Court ultimately rules like the D.C. Circuit Court and strikes subsidies moving forward, based on current legal precedent, individuals that currently have, or will receive a subsidy in the future, will likely not have to repay those subsidies retroactively, assuming that the individuals were legal eligible for the subsidy at the time of receipt.
- Current special enrollment rules remain in place and Exchange open enrollment will begin on November 15, 2014, as planned.
- The individual and employer mandates remain effective; employer compliance with the employer mandate is unchanged.

The availability of federal subsidies may have significant implications for employers as a result of the ACA's employer mandate. Under the employer mandate, large employers may face penalties if they do not offer coverage that meets certain requirements to their full-time employees. However, penalties apply only if an employee receives a subsidy to buy coverage through an Exchange. If the subsidy is available only in state-based Exchanges, employers would not be subject to penalties for employees living in states with an FFE.

### Other Lawsuits

Other lawsuits challenging the subsidies in states with FFEs are still pending in federal courts. These conflicting rulings mean that this issue will likely be appealed to the U.S. Supreme Court later this year.

The health care reform law—the Affordable Care Act (ACA)—has many complex requirements for employers and health plans. Please contact Kapnick Insurance Group with any questions about how you can prepare for any of the health care reform requirements. This Kapnick Insurance Group Update is not intended to be exhaustive nor should any discussion or opinions be construed as legal or tax advice. The information contained in this communication is intended to provide general information regarding health care reform and related topics, and is based on general information available at the time it was prepared. Readers should contact their tax and/or legal counsel for advice that is appropriate to their specific circumstances. This information cannot be used by any taxpayer to avoid tax penalties.

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