



NAVIGATING HEALTHCARE REFORM

July 23, 2014

ACA In The News: Federal Courts Issue Conflicting Rulings on Subsidies

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.



On July 22, 2014, two federal appeals courts—the District of Columbia Circuit Court and the 4th U.S. Circuit Court—issued conflicting rulings on the availability of subsidies in states with FFEs.

- 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 text of the ACA clearly restricts the subsidies 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**.

Health Insurance Subsidies

The 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: premium tax credits and 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, the 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.

The ACA delegated primary responsibility for establishing the Exchanges to individual states. However, because the U.S. Congress cannot require states to implement federal laws, the ACA provides that HHS will operate the FFE in any state that refuses or is unable to set up an Exchange, such as Florida.

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.

Court Decisions

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 the ACA. They assert that, according to the law's plain language, the ACA only authorized subsidies to be provided in states that have established their own Exchanges.

In *Halbig v. Burwell*, a three-judge panel from the D.C. Circuit Court **struck down the IRS' rule** that authorizes subsidies in all states, including those with FFEs. The court concluded that the ACA "unambiguously restricts" the subsidies to insurance purchased on Exchanges established by the states. Thus, the court said that subsidies are only available to individuals who obtain insurance through state-based Exchanges.

In *King v. Burwell*, the 4th Circuit Court ruled that the text of the ACA is ambiguous and subject to multiple interpretations. The court **upheld the IRS' rule** that authorizes subsidies in all states, including those with FFEs, as a permissible exercise of the agency's discretion. Thus, the court said that the subsidies are available to individuals who obtain insurance through either state-based Exchanges or through FFEs.

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.

Impact on Employers

Following the appellate court rulings, the Obama administration indicated that federal subsidies will continue to be available to eligible individuals in all states, including those with FFEs.

This availability of 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. In addition, although the U.S. Supreme Court has not yet agreed to consider it, it may decide to take up the issue in the future.