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On Wednesday, March 4, 2015, the U.S. Supreme Court will hear oral arguments in King v. Burwell, with a decision expected in late June. At issue in the case is the legality of an Internal Revenue Service (IRS) decision to extend tax credits to people who purchased their health insurance plans from the federal Exchanges set up in the 34 states that refused to set up state Exchanges authorized by the Patient Protection and Affordable Care Act (ACA) (P.L. 111-148). In a nutshell, the case will turn on the ACA language that ties the amount of tax credits to a health plan purchased “through an Exchange established by the State.” The petitioners contend that this language is unambiguous and clearly means that persons who purchased their health insurance plan through a federal Exchange do not qualify for tax credits. The government disagrees with the petitioners’ interpretation of the language, but argues that even if the language is unambiguous, the IRS’ decision is entitled to deference.

The importance of King v. Burwell. King v. Burwell has major significance because the uncertainty over this ACA language means that: (1) millions of people have no idea if they may rely on the IRS’s promise to subsidize their health coverage purchased through federal Exchanges, or if that money will be clawed back; (2) employers in 36 states have no idea if they will be penalized under the ACA’s employer mandate, or are effectively exempt from it; (3) insurers have no idea if their customers will pay for health coverage in which they enrolled, or if large numbers will default; and (4) the U.S. Treasury has no idea if the billions of dollars it is spending each month on federal Exchange subsidies were actually authorized by Congress.

Background. The ACA’s subsidy provisions are the key instrument through which the Act makes coverage affordable to individuals who purchase insurance on an Exchange. The ACA provides for advance payment of premium tax credits for people with incomes between 100 and 400 percent of the federal poverty level (FPL, $11,770-$47,080 for an individual in 2015) and cost-sharing reductions for people with incomes from 100 to 250 percent of the FPL ($11,770-$29,425 per year for an individual in 2015). To illustrate the importance of the subsidy provisions, according to an HHS Assistant Secretary for Planning and Evaluation (ASPE) Issue Brief, in 2015, 87 percent of people who selected a plan in states with a federal Exchange received premium tax credits.

Section 1311 of the ACA is the provision that allows states to set up Health Insurance Exchanges and section 1321 requires the Secretary of HHS to set up federal Exchanges in states that fail to set up Exchanges. Under section 1401 of the ACA, individuals are offered premium assistance through tax credits if they meet certain requirements, including enrollment “through an Exchange established by the State under section 1311.”

Despite the plain language of section 1401, the IRS began issuing tax credits through both federal and state Exchanges in January 2014 (26 C.F.R. Sec. 1.36B-1(k); 77 FR 30377, May 23, 2012) (the “IRS Rule”). The IRS Rule provides that the credits shall be available to anyone “enrolled in one or more qualified health plans through an Exchange,” and then adopts by cross-reference an HHS definition of “Exchange” that includes any Exchange, “regardless of whether the Exchange is established and operated by a State…or by HHS” (26 C.F.R. Sec. 1.36B-2; 45 C.F.R. Sec. 155.20).

Who are the King petitioners? The petitioners in King are Virginia residents who do not want to purchase comprehensive health insurance. Since Virginia has declined to establish a state Exchange, it is served by a federal Exchange. The petitioners allege that the cost of the least expensive unsubsidized Exchange plan through the federal Exchange would exceed 8 percent of their 2014 income, making them exempt from the ACA tax for failing to comply with the individual mandate. However, if the IRS Rule is correct and premium tax credits are applicable to federal Exchanges, the reduced costs of the policies available to the petitioners may subject them to the minimum coverage penalty. Therefore, if the IRS Rule is upheld, the petitioners contend they will
incur some financial cost because they will be forced to either purchase insurance or pay the individual mandate penalty.

Petitioners’ complaint. The petitioners contended in federal district court that the ACA’s statutory language precludes the IRS’s interpretation that the premium tax credits are also available on federally-facilitated Exchanges. On February 18, 2014, the district court dismissed their complaint, finding that the ACA as a whole clearly evinced Congress’s intent to make the tax credits available in both state and federal Exchanges (see Subsidies for health coverage through Exchanges within authority of IRS, February 26, 2014).

On appeal. On July 22, 2014, a three-judge panel of the Fourth Circuit unanimously affirmed the district court’s ruling that the IRS decision was a permissible exercise of administrative discretion, finding that the applicable statutory language was ambiguous and subject to multiple interpretations (see Appellate court creates circuit split by upholding IRS Rule, July 22, 2014).

That same day, in Halbig v. Burwell, the U.S. Court of Appeals for the District of Columbia Circuit reached the opposite conclusion, ruling 2-1 that the IRS did not have the right to rewrite the wording of the law to suit its intent to allow federal Exchange subsidies (see Federal appeals court axes subsidies for federally-run Health Insurance Exchanges, July 22, 2014). The White House then filed a motion for rehearing of the Halbig ruling before a full panel of the D.C. Circuit, which has seven judges appointed by Democratic presidents and four appointed by Republicans (see Halbig panel was wrong; Government seeks rehearing to avoid ‘perverse consequences’, August 6, 2014). The plaintiffs in Halbig opposed the motion for rehearing by the full D.C. Circuit, relying for the most part on the fact that the plaintiffs in King v. Burwell had already petitioned the Supreme Court for review in that factually related case (see Halbig team asks to skip straight to SCOTUS, August 20, 2014).

The D.C. Circuit granted the government’s motion for a rehearing of the Halbig appeal by the full panel of judges (see Halbig decision on premium subsidies to be reheard by full D.C. Circuit, September 10, 2014). However, after the Supreme Court agreed to review King v. Burwell, the D.C. Circuit ordered that Halbig be removed from the oral argument calendar and held in abeyance pending the Supreme Court’s decision in King v. Burwell (see Federal court waits for SCOTUS to rule on health insurance subsidy, November 19, 2014).

Do the King petitioners have standing? Recently, some news reports have questioned whether the King petitioners are eligible for Exchange subsidies and therefore legally eligible to challenge the IRS rule. Articles by the Wall Street Journal, on February 6 and February 9, 2015, and a Mother Jones article report that two of the petitioners might be eligible for veterans’ health coverage, which would make them ineligible for Exchange subsidies, another petitioner’s 2014 income may have been too low to qualify for Exchange subsidies since she turns 65 and will be qualified for Medicare before the Supreme Court rules, and another may not live in a federal Exchange state and may also be destitute and therefore unlikely to be required to buy even subsidized insurance under the ACA. The parties’ Supreme Court briefs do not address the question of petitioners’ standing and the Supreme Court has not ordered supplemental briefing on the question. The Justices, of course, are entitled to address the issue of standing during oral arguments.

Likely legal analysis by SCOTUS. To determine if an agency’s administrative action is valid, a court uses a two-part analysis as set forth in Chevron USA, Inc. v. Natural Resources Defense Council, 467 U.S. 837 (1984). First, the court asks whether the statutory language used by Congress clearly authorizes the rule issued by the agency. If the statute is clear, the inquiry ends, because the courts and agencies must “give effect to the unambiguously expressed intent of Congress.” If the statute is silent or ambiguous regarding the specific point, the court decides whether the agency interpretation is “based on a permissible construction of the statute.” If the agency’s interpretation of an ambiguous statute is reasonably within its discretion, then the court defers to the agency’s rule.

The Supreme Court briefs of both the petitioners and the government focus the majority of their arguments on the first part of the legal analysis. The petitioners contend that the ACA is clear that subsidies are available only in state Exchanges, while the government contends that the ACA is clear that subsidies are available in all Exchanges, including states with a federally facilitated Exchange. In the second part of the legal analysis, the
petitioners argue that deference to the IRS’ interpretation of the statute is inappropriate, while the government argues that the Court should defer to the IRS’ rule.

Petitioner’s brief. In their Supreme Court brief, the petitioners first argue that there is no legitimate way to construe the phrase “an Exchange established by the State under section 1311” to include one “established by HHS under section 1321.” Therefore, since Congress expressly provided tax credits only for state Exchanges, and not federal Exchanges, they argue that the court must give effect to that plain meaning of the ACA.

The petitioners concede in their brief that tax credits are important to the ACA’s statutory scheme, but argue that conditioning subsidies on state creation of Exchanges is not contrary to that scheme, any more than the ACA’s conditioning of Medicaid funds on state expansion of Medicaid eligibility was contrary to Congress’ obvious desire to extend Medicaid funds to all states. To further prove the point that Congress reasonably expected states not to reject the chance to provide their citizens with billions of dollars in tax credits, the petitioners point out that when the IRS Rule eliminated the incentive to set up state Exchanges by providing the tax credits to federal Exchanges, most states declined to set up the state Exchanges.

The petitioners also argue that the pre-ACA debate shows that Congress tied the availability of tax credits to state cooperation in setting up the Exchanges. In fact, a draft Senate bill did just that, and a House bill without incentives was a non-starter in the Senate for that reason.

The petitioners reject the government’s contention that giving section 1401 its plain meaning would lead to anomalous results as to other provisions of the ACA. The anomalies are simply contrived by the government, according to the petitioners, because all of the ACA’s other provisions are just as compatible with the plain meaning as with the government’s allegedly unlawful revision of it.

Finally, the petitioners argue that deference cannot save the IRS Rule for three reasons. First, Congress would never have delegated a decision of such economic and political significance to the IRS. Second, deference is inapplicable here because tax credits must be unambiguous, i.e., the Constitution itself demands that congressional authorization must be plainly stated where the expenditure of Treasury funds is at stake. Third, the IRS is never afforded deference in construing critical language that is not found in the Internal Revenue Code (Title 26 of the U.S. Code), and the critical language at issue in King is found in Title 42 of the U.S. Code, which governs the public health and welfare.

Government’s brief. The government’s brief argues that the ACA text, structure, and history demonstrate that tax credits were meant to be available through both state and federal Exchanges.

The government contends that the phrase “an Exchange established by the State” is merely a term of art that includes both an Exchange a state establishes for itself and an Exchange HHS establishes for the state (ACA sec. 1401). In addition, it argues that the phrase “shall…establish and operate such Exchange within the state,” which allows HHS to set up an Exchange if the state does not, conveys that an HHS-established Exchange is merely a statutory surrogate fulfilling the requirement that each state establish an Exchange (ACA sec. 1321). Therefore, according to the government, all Exchanges are Exchanges established by the state. The government offers numerous other textual references to confirm their interpretation and claims that the petitioners largely ignore the contradictions, anomalies, and absurdities their interpretation would create in other provisions of the Act.

The government provides two arguments in support of its claim that the ACA’s structure and design confirms that tax credits are available in all Exchanges: (1) tax credits are essential to the Act’s nationwide insurance-market reforms; and (2) the availability of tax credits in every state is essential to the Act’s model of cooperative federalism, meaning that the Act should be interpreted to avoid the disrespect for state sovereignty inherent in the petitioners’ interpretation of the Act.

The government also makes three arguments to show that the history of the ACA supports its position. First, it was well understood when the Act was passed that some states would not establish Exchanges for themselves. Second, the Act’s tax credits are not structured as a conditional-spending program designed to induce the states to establish Exchanges. Rather, they are federal tax credits provided to individual federal taxpayers as
an integral part of national reforms that apply whether or not the states act. Third, the ACA’s legislative record confirms that tax credits are available in every state.

Finally, the government argues that even if there is some question as to whether persons who purchased health insurance through the federal Exchanges were entitled to tax credits, the IRS is entitled to deference in its interpretation. The government noted that the IRS Rule was adopted after notice-and-comment rulemaking, which was conducted pursuant to an express delegation of authority to implement the ACA’s tax credit provisions.

**Effect of a ruling for the government.** If the Supreme Court rules for the government, the IRS Rule authorizing premium subsidies in all Exchanges will remain in effect, and premium tax credits currently available for all individuals will continue regardless of whether they are enrolled in a plan in a state Exchange or in a federal Exchange.

**Effect of a ruling for the petitioners.** If the Supreme Court rules for the petitioners and finds the IRS Rule invalid, individuals in the 27 states presently relying on a federal Exchange and the seven states with a state-federal partnership Exchange would lose access to premium subsidies. Without premium tax credits, enrollees may be forced to drop coverage, resulting in a smaller pool of enrollees in these federal Exchanges. The remaining enrollees would likely be those with more serious health conditions who would be more expensive to insure. This smaller pool of enrollees, with higher health costs, could lead to insurers ceasing to participate in the Exchanges.

In addition, invalidating the IRS Rule would essentially eliminate the requirement that large employers offer coverage to full-time employees in these states. This is because the penalty associated with the employer mandate is triggered when a full-time employee is not offered employer-sponsored coverage and qualifies for an Exchange premium or cost-sharing subsidy. Therefore, if Exchange subsidies are unavailable in states with a federal Exchange, the penalty against a large employer that fails to offer coverage is not triggered.

However, while a ruling for the petitioners could have significant policy implications for states with federal Exchanges, because *King v. Burwell* is not a constitutional challenge to the ACA, a decision invalidating the IRS Rule will not invalidate other parts of the law. For example, a ruling for the petitioners will not affect the subsidies for state Exchanges or the Medicaid expansion provisions of the ACA.

**Additional information.** Numerous articles on the *King* and *Halbig* cases have been written for *Health Law Daily* and *Health Reform WK-EDGE* by our health law analysts. These articles provide additional background on the history of the ACA subsidy provisions, Congressional intent, the lawsuits, what state officials believed about the subsidies, how the court decisions have created uncertainty for employers and individual enrollees, and possible legislative action at the state and federal level if the IRS Rule is invalidated.

- **Premium tax credits from federal Health Insurance Exchanges—Linchpin or loophole?** (August 27, 2014)
- **Halbig v. Burwell: Review options, potential ACA impact, and offering an alternative** (September 3, 2014)
- **Halbig and King decisions create uncertainty for employers** (September 3, 2014)
- **Don’t know much about history: how the creation of the ACA informs King v. Burwell** (January 21, 2015)

**Stay tuned.** Subscribers should stay tuned to *Health Reform WK-EDGE* and *Health Law Daily* for an upcoming Alert analyzing the parties’ oral arguments and their responses to the Justices’ questions.

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