

# Employee Benefits, ERISA & Executive Compensation Client Alert



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## US Supreme Court Upholds IRS Interpretation of ACA Subsidy Structure

In [King v. Burwell](#), the U.S. Supreme Court held that federal tax credits created by the Affordable Care Act (ACA) are available to individuals who purchase health insurance coverage from a federal or state established Health Insurance Exchange (“Exchange”).

**Background:** Section 1311 of the ACA provides that individuals and small business employers may purchase health insurance through an Exchange. Individual states may establish and operate their own Exchanges. However, if an individual state declines to establish an Exchange, then the federal Department of Health and Human Services will establish an Exchange within such state. The ACA also added Internal Revenue Code (“Code”) § 36B, providing premium tax credits to eligible individuals who purchase coverage through an Exchange “*established by a State*” pursuant to Section 1311 of the ACA. In connection with the addition of Code § 36B, the IRS issued regulatory guidance interpreting the phrase “*established by the State*” to mean “*established by the State or federal government.*” The IRS found this to be a reasonable interpretation of Code § 36B because a plain reading of the phrase “*established by the State*” would make federal tax credits unavailable to individuals in states with federally established and operated Exchanges. Without the tax credits, insurance coverage for individuals in those states would be unaffordable, which the court found to be inconsistent with congressional intent in enacting the ACA.

In [King v. Burwell](#), ACA opponents argued that the premium tax credits under Code § 36B may only be available to individuals purchasing health insurance on an Exchange “*established by the State.*” The Fourth Circuit Court of Appeals rejected this plain meaning argument; however, the D.C. Court of Appeals accepted a similar argument in another case. The U.S. Supreme Court agreed to hear the ACA opponent’s appeal in [King v. Burwell](#). The Supreme Court’s decision in [King v. Burwell](#) is significant to both individuals and employers, because a successful plain meaning argument would effectively absolve large employers from the ACA’s Shared Responsibility penalty if they fail to provide affordable health care coverage with respect to individuals in the 34 states with federally run Exchanges.

**Supreme Court Decision:** The majority opinion held that the phrase “*established by the State*” in Code § 36B must be interpreted to mean that premium tax credits are available to individuals through Federal or State established Exchanges. The majority explained that a plain meaning interpretation was not appropriate in this instance, and that the phrase must be read in context of the ACA’s entire structure and its other provisions. Interpreting the phrase “*established by the State*” literally, and out of the ACA’s structure and context, would cause a result that Congress plainly meant to avoid. Justice Roberts wrote that “Congress passed the

Affordable Care Act to improve health insurance markets, not to destroy them. If at all possible, we must interpret the Act in a way that is consistent with the former, and avoids the latter.”

**Implication:** The majority’s decision in [King v. Burwell](#) resolves the latest challenge to the ACA, with no other cases likely to reach the Supreme Court in the near future. Coupled with its previous ruling in [National Federation of Independent Business v. Sebelius](#), the ACA has survived largely unscathed (the ACA mandate requiring states to expand Medicaid was struck in the National Federation of Independent Business case). Individuals in all states may continue to receive premium tax credits for insurance purchased on federally run Exchanges. Additionally, employers should continue to ensure they are compliant with the numerous statutory and regulatory requirements under the ACA to avoid any potential excise taxes, even if they only operate in states with federally run Exchanges.

-- [Ricardo Carlo](#), [Eric Loi](#), and [Tim Brechtel](#)

*Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, you may also contact:*

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