

U.S. Supreme Court Takes Up Major Challenge to Federal Health Reform

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Are Employers in the 34 States Without Exchanges Subject to Penalties?

Despite the fact that there is no longer any disagreement in the lower courts, the Supreme Court on Friday, November 7, 2014, made the unusual and highly unexpected move of agreeing to rule on a key challenge to federal health reform.

As discussed in two prior eblasts ([Health Reform News](#); [Dueling Districts Challenge Health Reform](#)), the controversy turns on a technical statutory issue in the tax code provisions of the ACA. The ACA's employer mandate penalties hinge on the availability of tax credits. An employer whose health plan fails certain standards of coverage or affordability standards is subject to a penalty if a full-time employee "enroll[s] . . . in a qualified health plan with respect to which an applicable tax credit . . . is allowed or paid with respect to the employee." Under the ACA, an applicable tax credit is available only for the purchase of insurance on an "Exchange established by the State under section 1311 of the [ACA]." However, the IRS adopted a rule interpreting the ACA to allow tax credits for insurance purchased on either a state- or federally-established Exchange.

Therefore, under the pure statutory language of the ACA, tax credits are unavailable for purchases through the federal Exchanges, and employers there face no penalties for failing to offer coverage. Under the IRS rule, however, the tax credit (and employer penalties) are given broader reach.

If the Supreme Court rules that subsidies are not available in federal exchanges, it could have extremely significant ramifications. Since both houses of Congress are now Republican-controlled, it is unlikely that the votes could be garnered to conform the ACA text to the IRS regulation. Absent a fix in Congress, states with exchanges may well abandon their exchanges so that local employers in their states would be shielded from the employer penalty. In addition, without a Congressional amendment, the federal tax subsidy may be invalidated, which could create a backlash against the individual mandate, and the entire basis for the health reform bill.

It is likely that the Supreme Court will rule at about the time the first tax credits could be taken (in April 2015), and well in advance of the time that the first penalties would be assessed (in April 2016). Stay tuned!

Date Created

November 10, 2014