

SUPREME COURT DECISIONS IMPACT ACA, SAME-SEX MARRIAGE

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Special Report

HIGHLIGHTS

- Code Sec. 36B Regs Upheld Nationwide
- Tax Credit Available In All Exchanges
- State Bans On Same-Sex Marriage Unconstitutional
- Same-Sex Couples On Par With Opposite-Sex Couples For Filing Returns

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Supreme Court Upholds Premium Assistance Tax Credit; Extends Same-Sex Marriage Nationwide

The U.S. Supreme Court has handed down two much-anticipated decisions: one on the Affordable Care Act's key provision, the Code Sec. 36B premium assistance tax credit; and another on same-sex marriage nationwide. In *King v Burwell, SCt, June 25, 2015 (2015-1 USTC ¶50,356)*, the Court ruled 6 to 3 that the Code Sec. 36B credit is available to enrollees in both federally-facilitated and state-run Exchanges (currently commonly referred to as Marketplaces). In *Obergefell v. Hodges, SCt, June 26, 2015 (2015-1 USTC ¶50,357)*, the Court ruled 5 to 4 that the Fourteenth Amendment requires a state to license a marriage between two people of the same sex and to recognize a marriage between two people of the same sex when a marriage was lawfully licensed and performed out of state. Both decisions have far-reaching tax consequences.

King v. Burwell: For individuals who claimed or intend to claim the Code Sec. 36B credit, the *King* decision answers the question of whether that credit would be available nationwide going forward, and equally important for many taxpayers, the issue of whether they would have to repay any credits already received. On a broader level, the Court saw its decision as preserving no less than the viability of the entire Affordable Care Act. "Congress passed the Affordable Care Act to improve health insurance markets, not to destroy them," Chief Justice John Roberts wrote for a united majority.

IMPACT. *Also of immediate concern, and definitely not going away now that the Supreme Court has spoken, are the myriad*

rules and compliance responsibilities and deadlines that remain in place for employers under the "employer mandate" and individuals under the "individual mandate."

COMMENT. *Many opponents of the ACA after the Supreme Court released its decision stated that the underlying health care/health insurance system under the ACA is going bankrupt and that it is only a matter of time until alternatives to the Code Sec. 36B credit and other "artificial" support structures will need to be replaced by other options.*

The *King* decision hands the Obama administration its second decisive victory on the ACA. The Supreme Court previously upheld the constitutionality of the 2010 health care reform legislation, including its linchpin individual mandate that requires individuals to pay a penalty if they fail to carry minimum essential health insurance (*National Federation of Independent Business, et al. v. Sebelius, SCt, 2012-2 USTC ¶50,423*).

Obergefell v. Hodges: Meanwhile, the U.S. Supreme Court's decision in *Obergefell* effectively ends the necessity for same sex-couples in states that did not recognize same-sex marriage to have to file as single individuals for state tax purposes but as married for federal tax purposes.

IMPACT. *Although the immediate changes under Obergefell involve state tax law and the requirement that all state taxing authorities recognize same sex marriage for filing status, federal tax law will be*

impacted not only as the result of changing strategies in coordinating federal and state tax planning, but also for determining the downstream changes required on previously-filed federal forms because of changes in itemized deductions for state taxes paid and other considerations where amended state tax returns are filed for past tax years.

CODE SEC. 36B PREMIUM ASSISTANCE CREDIT

The Affordable Care Act (officially known as the Patient Protection and Affordable Care Act of 2010) introduced numerous health insurance market reforms, such as the prohibition on insurers from denying coverage to individuals with preexisting health conditions. To prevent individuals from driving the cost of health premiums up by waiting until they became ill to obtain insurance—something that had occurred in the past—the ACA required all individuals to obtain health insurance unless they fell below a certain income threshold.

To facilitate the purchase of health insurance, the ACA provided for the creation of Health Insurance Exchanges (also referred to as “Marketplaces”) in each state. If a state elected not to create an Exchange, the ACA provided that the federal government would create and operate an Exchange in that state.

The ACA provided that certain individuals who enrolled in health coverage through “an Exchange established by the State” would be eligible to receive the Code Sec. 36B premium assistance tax credit.

The main issue in question in *King* was whether the millions of individuals who had obtained health insurance from one of the Exchanges established by the Federal government rather than “by a State” were eligible to receive the Code Sec. 36B premium assistance tax credit under the ACA.

COMMENT. *Only enrollees in Exchange coverage can claim the Code Sec. 36B credit, and only then if they qualify. This*

remains unchanged after the Supreme Court’s decision. Individuals who obtain insurance through their employers are ineligible for the tax credit.

COMMENT. *Twenty-seven states have Exchanges/Marketplaces established and run entirely by the federal government (federally-facilitated Exchanges). Seven more states maintain partnership Exchanges, which the U.S. Department of Health and Human Services (HHS) treats as federally-facilitated Exchanges. Three states have federally supported state-based Marketplaces, which rely on the IT platform of federally-facilitated Exchanges.*

“Congress passed the Affordable Care Act to improve health insurance markets, not to destroy them,” Chief Justice John Roberts

General requirements. Generally, to be entitled to a Code Sec. 36B credit, an individual must not have access to affordable coverage through an eligible employer plan that provides minimum value, must not be eligible for coverage through Medicaid or another government program, and must have household income between 100 percent and 400 percent of the federal poverty line for their family size.

IRS regulations. The IRS issued final regulations under Code Sec. 36B in 2012 (TD 9590). The regulations allow enrollees in state-run Exchanges and federally-facilitated Exchanges to claim, if eligible, the Code Sec. 36B credit. The IRS made no distinction between individuals with coverage through state-run or federally-facilitated Exchanges for purposes of the Code Sec. 36B credit if the individual would be otherwise eligible to claim the credit.

Litigation. In the case that ultimately reached the Supreme Court, the taxpayers

argued that the IRS regulations were contrary to the ACA. A federal district court rejected the taxpayers’ argument, as did the Court of Appeals for the Fourth Circuit in July 2014. Other courts, including the District of Columbia Court of Appeals, which issued its decision in *Halbig v. Burwell*, CA-D.C., 2014-2 *ustc* ¶50,366 on the same day as the Fourth Circuit, took contrary positions. As a result of the Circuit split between *King* and *Halbig*, the Supreme Court agreed to review the Fourth Circuit’s decision and heard oral arguments in March 2015.

SUPREME COURT’S KING DECISION

Writing for the majority in *King*, Chief Justice Roberts found that Code Sec. 36B’s premium assistance tax credits are not limited to individuals who live in states that have established health insurance Exchanges. Rather, they are also available to qualifying individuals who enroll in an insurance plan in states that have federally-facilitated Exchanges.

IMPACT. *This decision turns back the most serious challenge to date regarding the continued viability of the ACA. An estimated 6.2 million individuals on federally-facilitated Exchanges who rely on the credit to make their insurance affordable were threatened, as were others whose insurance premiums would have risen as many previously-insured people dropped out of the system.*

At the heart of the controversy was interpretation of the statutory language within Code Sec. 36B: “an Exchange established by the State under [42 U.S.C. §18031]” should be read to include Federal Exchanges. “The context and structure of the Act compel us to depart from what would otherwise be the most natural reading [of this statutory phrase],” the Court concluded.

Not IRS’s call

Although the Court upheld what the IRS regulations did in allowing the credit, it did not defer to the IRS’s right to decide. Given

the ambiguity within Code Sec. 36B, and the importance of the credit as one of ACA's key reforms "involving billions of dollars ...for millions of people," there was no implicit delegation of authority to the IRS by Congress to fill in any gaps in drafting the ACA. The Court reasoned, "...it is especially unlikely that Congress would have delegated this decision to the IRS, which has no expertise in crafting health insurance policy of this sort."

IMPACT. *In rejecting application of the so-called Chevron rule for determining the level of deference owed to the IRS's regulatory authority, the Court may have indirectly prevented post-Obama administrations from using regulations to chip away at the ACA.*

Ambiguous language

The Court decided that the language of Code Sec. 36B was not plain on its face, given the place that Code Sec. 36B served within the "overall statutory scheme." The majority was unconvinced by the argument that the phrase "established by the State" would be unnecessary if Congress meant to extend tax credits to both State and Federal Exchanges. It instead saw clarity as a particular problem to determining a fair construction of the Affordable Care Act, which "contains more than a few examples of inartful drafting."

Broader view

Given the Court's view that the language of the Code Sec. 36B credit was ambiguous, the majority then felt justified in looking to "the broader structure of the Act to determine the meaning of Section 36B." The majority rejected a literal reading of Code Sec. 36B because it would "destabilize the individual insurance market in any State with a Federal Exchange, and likely create the very "death spiral" that Congress had designed the Act to avoid.

"Death spiral"

The Court saw a parallel between an unfavorable holding on Code Sec. 36B and the

lessons learned from insurance market regulation undertaken by several States in the 1990s. A two-part system of guaranteed issue and community rate-setting within those States had encouraged too many people to wait until they were ill to purchase insurance. That created a "death spiral" in which premiums rose, the number of healthy people buying insurance declined and fewer people were left to pay for sicker people. The Court viewed the missing component in those insurance markets, but not in the later, successful Massachusetts system on which the structure of the ACA was based, to be the requirement that all individuals obtain insurance and the availability of tax credits that made insurance affordable.

COMMENT. *Without providing for a tax credit (Code Sec. 36B) to participants on Federal Exchanges, the other intertwined pillars of health care reform would collapse, causing an economic "death spiral." Collapse of this interlocking structure was not intended by Congress in enacting the Affordable Care Act, the majority reasoned: "It is implausible that Congress meant the Act to operate in this manner."*

Summing up

Chief Justice Roberts ended the majority opinion with a concession to the dissenting Justices, admitting that the "plain-meaning arguments are strong." However, the majority concluded that, nevertheless:

"The Act's context and structure compel the conclusion that Section 36B allows tax credits for insurance purchased on any Exchange created under the Act. Those credits are necessary for the Federal Exchanges to function like their State Exchange counterparts, and to avoid the type of calamitous result that Congress plainly meant to avoid."

Dissent. Justice Scalia dissented, joined by Justices Thomas and Alito: "It is hard to come up with a reason to include the words "by the State" other than the purpose of limiting credits to State Exchanges." Scalia viewed the majority opinion as repairing a

law, rather than merely exercising its power to pronounce the law as Congress has enacted it. To underscore that the majority has in fact rewritten the law, Scalia suggested, "We should start calling this law SCOTUScare."

What's Next

The Supreme Court's decision in favor of the Code Sec. 36B credit does not end the uncertainty over the Affordable Care Act's long-term future, or even the short-term survival of some of its provisions. Many within the GOP in particular will continue to press for the full repeal of "Obamacare." A GOP sweep of the White House and Congress in 2016 could bring passage of an entirely different health-care law, or give rise to amendments that would transform the ACA dramatically.

As the public becomes increasingly accustomed to some of the beneficial aspects of the ACA, however, consensus is growing that full repeal will become extremely difficult to legislate. On the other hand, momentum for some fine-tuning has been increasing: the medical device excise tax has been gathering opponents on both sides of the aisle on Capitol Hill; and pressure has been increasing to raise the hours-per-week cutoff for defining an eligible employee, as well as to delay the excise tax on "Cadillac" plans.

IMPACT. *The impact of the decision reaches beyond enrollees in the Health Insurance Exchanges. The Code Sec. 36B credit affects both the individual shared responsibility requirement (individual mandate) and the employer shared responsibility provisions (employer mandate).*

SAME-SEX MARRIAGE

In *Windsor, 2013-2 USTC ¶50,400*, the Supreme Court held that Section 3 of the federal Defense of Marriage Act (DOMA) was unconstitutional. Section 3 of DOMA provided that marriage for federal purposes was only the union between members of the opposite sex. The Supreme Court did not -- in 2013 -- reach the question of whether same-sex couples had a constitutional right to marry.

Supreme Court's Obergefell Decision

Writing for the majority in *Obergefell*, Justice Kennedy said that “the Fourteenth Amendment requires a State to license a marriage between two people of the same sex and to recognize a marriage between two people of the same sex when their marriage was lawfully licensed and performed out-of-State.” Kennedy explained that the right to personal choice regarding marriage is inherent in the concept of individual autonomy. Like choices concerning contraception, family relationships, procreation, and childrearing, all of which are protected by the Constitution, decisions concerning marriage are among the most intimate that an individual can make.” Kennedy further noted that same-sex couples have the same right as opposite-sex couples to enjoy intimate association. “Excluding same-sex couples from marriage thus conflicts with a central premise of the right to marry.”

Turning to the Fourteenth Amendment, Kennedy wrote that “the right of same-sex couples to marry that is part of the liberty promised by the Fourteenth Amendment is derived, too, from that Amendment’s guarantee of the equal protection of the laws. It is now clear that the challenged laws burden the liberty of same-sex couples, and it must be further acknowledged that they abridge central precepts of equality. Here the marriage laws enforced by the respondents are in essence unequal: same-sex couples are denied all the benefits afforded to opposite-sex couples and are barred from exercising a fundamental right. The Equal Protection Clause, like the Due Process Clause, prohibits this unjustified infringement of the fundamental right to marry.”

COMMENT. *Because the Court held that same-sex couples could exercise the right to marry in all states, it further held that there is “no lawful basis for a State to refuse to recognize a lawful same-sex marriage performed in another State on the ground of its same-sex character.”*

Dissent. Four justices dissented. The dissenting judges noted that “Under the Constitution, judges have power to say what the law is, not what it should be. Although the policy arguments for extending marriage to same-sex couples may be compelling, the legal arguments for requiring such an extension are not. The fundamental right to

“The Fourteenth Amendment requires a State to license a marriage between two people of the same sex and to recognize their marriage ...,” Justice Anthony Kennedy

marry does not include a right to make a State change its definition of marriage. The people of a State are free to expand marriage to include same-sex couples, or to retain the historic definition.”

COMMENT. *Before Windsor, the IRS was precluded by Section 3 of DOMA from recognizing same-sex marriage for federal tax purposes. Windsor required federal recognition. The Supreme Court’s decision in Obergefell on the other hand technically changes nothing on the federal*

tax level, regarding the treatment as set out by the IRS in Rev. Rul. 2013-17 – the state of celebration controls. However, it does remove complexities faced by same-sex couples in coordinating planning and compliance considerations under federal and state tax laws when joint returns (or married, filing separately) were not allowed at the state level.

COMMENT. *The IRS is expected to update its guidance in Rev. Rul. 2013-17 to remove language that refers to some states not recognizing same-sex marriages. Specifically, Rev. Rul. 2013-17 stated that the state-of-celebration controlled for federal purposes, “even if the state in which they are domiciled does not recognize the validity of same-sex marriages.”*

IMPACT. *Conceivably, some same-sex couples benefitted from being able to file as single at the state tax level while filing jointly for federal tax purposes. That benefit has ended.*

IMPACT. *Same-sex married couples within certain states who had to file as single individuals for state tax purposes now have a Constitutional right to file amended returns as married at the state level. Whether the normal three-year limitations period for filing these amended returns will apply remains to be tested. Also uncertain may be whether same-sex married couples must now retroactively file jointly or whether re-filing will be made optional, either state-by-state or nationwide.*

IMPACT. *The state tax paid on amended state returns may also impact the amount of federal itemized deductions claimed for state income taxes.*