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NEWSLETTER

Supreme Court Decision Upholding Affordable Care Act Affirms Contracting Opportunities in Insurance Exchanges and Medicaid

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In the July 16, 2012 edition of Bloomberg BNA's *Health Care Policy Report*, Wiley Rein attorneys Jim Slattery, Kathryn Bucher, Daniel P. Graham and Kate R. McDonald published an article on the implications for health care contractors of the Supreme Court's decision in *Nat'l Fed'n of Indep. Bus. v. Sebelius*, No. 11-393, slip op. (U.S. June 28, 2012). That decision affirmed the individual mandate in the Patient Protection and Affordable Care Act (ACA), Pub. L. No. 111-148, 124 Stat. 119 (2010), and preserved Medicaid expansion, albeit at the option of each state. As a result, the decision helps secure opportunities ahead for entities that will contract with states and the federal government to build insurance exchanges or underwrite Medicaid managed care plans. Contractors should be cautiously optimistic about the future and yet take precautions to secure contractual protections against political reversals.

The full scope of these opportunities is not yet known for several reasons. First, regardless of the Supreme Court's decision, the November elections for the Senate and White House will determine the future of health care reform, as Governor Romney has pledged to begin working to repeal the ACA on his first day in office. The path forward will also be shaped by critical fiscal pressures that will force painful decisions in the coming months and years. The combined effect of the expiration of the Bush tax cuts, the payroll tax cut, the need to raise the debt ceiling in late 2012 or early 2013 and the automatic spending cuts required under the Budget Control Act of 2011 (BCA), Pub. L. No. 112-25, 125 Stat. 240 (2011), including sequestration, will put enormous political pressure on Congress to cut

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spending. Budget experts know that spending cannot be effectively controlled without containing the costs of Medicare, Medicaid, Veterans Health Care and other federal health care-related outlays. As the law is currently written, however, much of the ACA spending would likely not be subject to the cuts required by the BCA. Many expenditures are specifically exempted from sequestration or capped by the BCA or earlier statutes. Moreover, for any given fiscal year in which sequestration is triggered, only new budget authority for that year is reduced—*i.e.,* funds that first become available for obligation in that year. Still, the sequestration process could apply to other programs created or impacted by the ACA and regardless of whether they were funded by direct (*i.e.,* mandatory) or discretionary spending.

Much of the new federal funding for Medicaid expansion is likely to go to managed care organizations (MCOs) currently providing Medicaid coverage to approximately 70% of Medicaid beneficiaries. Many governors in both political parties have concluded that managed care is a cost-efficient way to deliver Medicaid without compromising quality of care. Democrats, who have historically been slow to embrace managed care, are accepting it as an alternative to the traditional fee-for-service reimbursement system and its exploding costs. As reported by *The Wall Street Journal,* WellPoint Inc.'s recent announcement that it will pay $4.46 billion to buy the Medicaid contractor Amerigroup Corp. underscores "the future of health coverage as a business that increasingly intertwines the roles of government and private companies."

Given that the Court granted all states the right to opt out of Medicaid expansion, the question turns to whether the states that fought the legislation will sign up for expansion. Pressure to do so will come from many sides. Hospital systems, provider associations and MCOs can be expected to make compelling cases for expansion by focusing on the anticipated savings from large reductions in uncompensated care, new corporate investment and corresponding job growth and an increase in corporate tax revenues. Whether those dollars—and any economic gains associated with a healthier low-income population—would be sufficient to offset the increased state expenditures for Medicaid expansion starting in 2017 is the subject of vigorous debate.

Health insurance exchanges present another growth opportunity for contractors, having been described as the "centerpiece" of the ACA. They are instrumental to the success of health care reform because they are expected to increase consumer access and expand coverage. The intent behind the Act was for small business owners and individuals who purchase their own coverage to benefit from reduced insurance premiums that would accompany enlarged risk pools. The development and implementation of these exchanges offer sizeable contracting opportunities to entities with the requisite experience and expertise, as states must have their exchanges in place by the start of 2014 unless this date is extended as some are advocating. Republican victories in the White House and the Senate could take many of these opportunities away. If the Democrats retain control, the opportunities only grow.

Under the ACA, states are required to have health insurance exchanges in place by the start of 2014. The Act specifies that funding for the exchanges will be allocated to the states on an annual basis by the Secretary of Health and Human Services (HHS). HHS has been making grants on an ongoing basis but will not award any grants after January 1, 2015. If a state elects not to establish an exchange or the Secretary determines that

the state has not made sufficient progress by January 1, 2013, to have the required exchange operational by the first day of 2014, then the Secretary will either establish an exchange within the state directly or implement one through agreement with a non-profit. In part due to the uncertainty surrounding the future of the ACA, states have made varying degrees of progress toward meeting the exchange requirement.

For current state grantees and contractors, the Supreme Court's decision means that performance under their respective exchange grants and contracts will move full speed ahead. The decision also will likely open up numerous additional opportunities with states that delayed work on the design and implementation of health insurance exchanges pending the decision. Many of these states will likely rush towards the November 16, 2012 deadline for submitting exchange blueprints to HHS and will undoubtedly rely on contractors to support that effort. A few states are still maintaining that they will wait for election results before beginning any work to build an exchange, possibly hoping for repeal of the ACA or the exchange requirement if Republicans take control of the Senate and White House, or an extension to the January 1, 2014 deadline for operational exchanges if Republicans do not take control.

Like many other ACA projects, grants to assist states in building and implementing exchanges are funded by appropriations. Such projects have already been the subject of efforts to "defund" the appropriation that can be expected to continue. Although the BCA exempts from sequestration unobligated balances carried over from prior fiscal years and this exemption likely protects grants to assist states in creating exchanges, Congress is expected to explore a variety of alternatives to sequestration. As a result, unobligated ACA funds for exchange development may be placed on the table as Congress attempts to right the country's fiscal problems.

There are steps contractors can take to prepare for and mitigate the effects of potential spending reductions before they occur. Of particular importance to contractors working with state grantees under the ACA are the following:

- **Availability of Funds Clauses.** Contracts with state grantees may contain a variety of provisions that limit the state's liability to available funding. Such provisions have been included in many state exchange contracts, for example, and some are far less forgiving than others. Contractors should inventory their contracts to understand how the risk of funding shortfalls has been allocated. Contractors should further ensure that their expenditures do not exceed the funds obligated by the state to the contract, particularly in large IT projects where costs can be front-loaded with substantial software license fees. In the event that expenditures exceed or are close to exceeding available funding, contractors should comply with any notice provisions in their contracts and otherwise document the grantee's knowledge and approval of the expenditure.
- **Termination and Changes Clauses.** If ACA programs are cut or scaled back, termination and changes clauses will likely be the vehicles used to achieve any savings. Again, these clauses vary by contract and by state and may be substantially different from standard federal clauses. Contractors should be cognizant of the distinction between a "partial" termination of the contract for convenience and a deductive change to the contract, and the potentially different remedies that may be available for

each.

- **Subcontractors, Vendors and Suppliers.** Contractors should review their agreements with their team members to ensure that their liability under these agreements is co-extensive with the state's liability for a lack of available funding, partial termination or deductive change.