

# Client Update

## Just a Bit of Clarity—Recent Developments Shine Some Light on Trump and GOP Plans for Healthcare Reform

### NEW YORK

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Since the 2016 election of President Trump and Republican majorities in both the House and the Senate, there has been a strong push to repeal and replace the Affordable Care Act (the “ACA”). However, there has been little detail as to what is meant by “repeal,” or “replace,” or when either will happen.

Two recent developments have provided some additional clarity, but leave many questions unanswered.

First, the Department of Health and Human Services (“HHS”) recently issued proposed rules that are designed to make it more attractive for health insurers to continue to offer plans to individuals and small groups that purchase health insurance on the ACA exchanges.

Second, *The New York Times* released a document that provides the outline of the House Republican leadership’s plans to “repeal” and “replace” the ACA (the “House GOP Plan”). The plan is consistent with the broad outlines for healthcare reform that Mr. Trump has previously proposed and provides the most concrete guidance to date on what healthcare reform in the Trump administration may look like. But the devil is in the details—many of which are still missing. Until specific details are provided about the subsidies contemplated by the Trump administration and GOP and how healthcare reform will be funded, it is impossible to fully assess how any changes will impact the number of people that are insured and able to purchase healthcare.

One thing remains clear: the changes contemplated by the Trump administration and congressional Republicans will have significant implications for every sector of the healthcare industry.

## SHORT-TERM BAND-AID: HHS PROPOSED REGULATIONS

On February 15, 2017, HHS proposed regulations governing certain aspects of ACA exchanges where millions of individuals and small businesses buy health insurance. Anyone purchasing health insurance using government subsidies must do so on an ACA exchange. If insurers abandon the ACA exchanges, many people relying on the government subsidies may effectively have no way to purchase health insurance. HHS is concerned that anticipation of ACA repeal may dissuade insurers from offering plans on the exchanges. Indeed, these proposed regulations were issued the day after Humana announced that it would no longer be offering insurance plans to be sold on the exchanges.

The new rules are designed to encourage insurers to continue offering plans on the exchanges in part by blunting concerns over adverse selection. Adverse selection occurs when people who know they will likely need healthcare purchase health insurance today, while people who are healthy today delay the decision to buy healthcare until their health deteriorates. The result is a sicker risk pool, which increases the cost to insurers of providing coverage. The proposed HHS rules seek to improve the risk pool and promote stability with four principal changes:

- ***Cut the open enrollment period in half.*** This makes it harder for people to hedge their bets by waiting until later to decide if they need healthcare. If someone misses the deadline to buy insurance, he or she would not be able to obtain coverage until the next open enrollment period. Thus, people that become sick during the time that is no longer part of the open enrollment period will now have to wait until the following year to purchase health insurance. The hope is that many people will not be willing to take the risk that they become sick during the lengthened off-period and will sign up earlier than they would otherwise.
- ***Impose stricter auditing of individuals seeking to enroll through special enrollment.*** Insurers have long complained that sick people abuse special enrollment rules as a way to purchase health insurance after the open enrollment deadline.
- ***Allow insurers to apply a premium payment to an individual's past debt owed for coverage from that same insurer.*** Under ACA's guaranteed issue rules, an insurer must offer health insurance to anyone that applies for coverage and pays the premium for the first month. Under current HHS rules, if a person has failed to pay premiums that she owes under one insurance plan and the following year seeks to enroll in a different insurance plan offered by the same health insurer, the insurer would have to enroll the

person in the new plan. The insurer is prohibited from applying newly offered premiums to unpaid premiums under the old plan. That allows people to game the system by failing to make premiums at the end of the year and switching to a different plan the following year. Under the new HHS rules, an insurer can condition its willingness to provide coverage under the new plan by requiring the person to both pay off unpaid premiums owed over the past year and make a premium payment for the current year. This removes incentives for people to pay insurance premiums only when they are sick and need healthcare.

- ***Allow insurers more flexibility in designing plans sold on the exchanges.*** Insurance plans that are sold on the exchanges are rated by “precious metals” that reflect—on an actuarial basis—the percentage of healthcare costs that the plan will pay. The new HHS regulations allow health insurers to increase “de minimis” variation in actuarial values. HHS hopes that proposal will give insurers greater flexibility in designing plans that make economic sense for both the insurer and insured.

These proposed rules are consistent with the Trump administration’s deregulatory approach to healthcare. The administration wants to make it easier for healthier people, and more costly for sick people, to buy health insurance.

### WHAT DOES REPEAL AND REPLACE ACTUALLY MEAN?

The House GOP Plan provides a blueprint for eliminating significant portions of the ACA and replacing them with a more market-oriented approach. The steps outlined in the blueprint should all be achievable through the budget reconciliation process, requiring only a majority of 51 votes in the Senate. Other provisions, such as the requirement that insurance coverage be available regardless of preexisting conditions, do not touch on the federal budget and therefore require a supermajority vote in the Senate to change. These provisions, which in many cases are popular, would remain intact.

The core of the House GOP Plan is to replace the ACA’s subsidies with a universal advanceable, refundable tax credit for anyone who does not receive health insurance through an employer or the government. The credit is advanceable because it is available when policy premiums are due (unlike a typical tax credit that applies only when taxes are filed). The credit is refundable because people who have a larger credit than tax bill receive a check from the government for the difference.

At first glance, the proposed tax credit looks similar to the ACA’s Advanced Premium Tax Credits, but it has key differences. The ACA credit was available

only to people with income less than 400% of the federal poverty level. The size of the ACA credit is not uniform—people with smaller incomes receive a larger credit than people with higher incomes. Under the House GOP Plan, the credit would be available to anyone. The size of the credit—which has not been announced—would depend only on age. While the ACA credit could be used only to purchase exchange plans, the new credit may be used to purchase any plan. In particular, these credits may be used to purchase “catastrophic care” plans—plans with low premiums but very high deductibles—which currently cannot be offered on exchanges. Such plans are attractive to young, healthy people that do not anticipate significant healthcare costs.

The House GOP Plan would increase the permitted level of contributions to health savings accounts (“HSAs”) and allow users greater discretion as to where they spend HSA funds. The House GOP Plan also calls for “State Innovation Grants,” which are funding that states could use to help fund the care of the sickest patients that have the greatest healthcare costs. The Plan, however, provides no information about how large these grants would be.

The House GOP Plan calls for repeal of a number of tax measures that have long drawn the GOP’s ire:

- the individual mandate, which is a penalty assessed on certain people who do not buy health insurance and penalties that are assessed on certain employers that do not offer health insurance to their employees;
- the “Cadillac tax” on high-cost health insurance plans;
- the so-called “medicine cabinet tax,” which is actually a prohibition against using money set aside in HSAs or flexible saving accounts to purchase over-the-counter drugs unless they are purchased pursuant to a prescription from a doctor;
- annual taxes of approximately \$3 billion imposed on the branded pharmaceutical industry;
- the excise tax on medical devices; and
- the increased threshold for deducting medical expenses.

While providing some details, the House GOP Plan leaves many questions unanswered. Most notably, it does not state how large the tax credit will be—leaving open the question as to whether it will be sufficient to allow low-income people to afford insurance. It also does not state how this credit or the tax repeals will be funded. The Plan does, however, speak approvingly of earlier GOP efforts to cap the size of the tax exclusion for employer-sponsored health insurance.

While liberal and conservative healthcare economists alike have long argued for such a cap, it would likely prove unpopular among employers and other key GOP constituencies.

### MEDICAID CUTBACKS LOOM

Prior to the enactment of the ACA, states were only required to offer Medicaid coverage for certain types of low-income people—principally children and their parents. The federal government reimbursed a certain percentage of the state's Medicaid expenses—somewhere between 50% to 80%, depending on the state. The ACA expanded Medicaid to cover childless adults with incomes up to 138% of the federal poverty level. For this “expansion” population, the federal government reimburses 90% of the state's Medicaid costs.

The House GOP Plan proposes that this Medicaid expansion would be entirely repealed after an unspecified period of time. States subsequently would be able to cover the “expansion” population—but only at the traditional federal government “match” rate.

The House GOP Plan would also curb Medicaid spending through a form of “block” grants. Currently Medicaid is an entitlement program, meaning that the federal government has an open-ended commitment to match a percentage of each state's spending. Many Republicans have sought to end Medicaid's entitlement status. Some have instead sought to offer “block” grants by giving each state a fixed amount per year—leaving the states to bear any additional costs of their Medicaid programs. Still others have sought a per capita approach, meaning that the federal government would provide a fixed amount per person, giving states greater protection in the event a recession caused more people to become unemployed. The House GOP Plan indicates support for this per capita approach.

If the Medicaid expansion is rolled back and any form of block grants is implemented, states could wind up bearing significantly more Medicaid costs. As Medicaid already strains many state budgets, a significant increase in the Medicaid costs that a state was forced to bear would leave the state with the option of restricting Medicaid eligibility, cutting spending or raising taxes. Given those options, many states likely would opt for reducing Medicaid eligibility.

It is far from certain, however, that the House GOP's Medicaid plans will be implemented. Several Republican senators in states with many Medicaid recipients are highly leery of any Medicaid cutbacks. With a thin GOP majority in the Senate, there may not be enough votes for significant Medicaid reform.

## WINNERS AND LOSERS

Although it is hard to assess the ultimate impact of healthcare reform until more details emerge, what we know now suggests that particular subsectors of the industry could be winners or losers:

### Medical Device Manufacturers

Healthcare reform will likely be a major boon to device manufacturers because there is strong GOP support for lifting the excise tax on devices. Device manufacturers may also benefit from greater flexibility in patients' ability to use HSA money on devices that would not typically be covered by insurance. That being said, device manufacturers may suffer lost sales to the extent people lose insurance coverage or purchase only thin coverage that leaves them unable to afford devices.

### Hospitals

To the extent healthcare reform results in significantly more uninsured patients, hospitals will likely bear increased costs. Because hospitals often treat patients regardless of ability to pay, more uninsured patients means increased charity care and bad debt writeoffs. This burden would fall heavily on Disproportionate Share Hospitals ("DSHs")—hospitals that treat a large percentage of the indigent population. The House GOP Plan, however, alleviates some of this burden by restoring the ACA's cutback on payments to DSHs.

### Pharmaceutical Industry

The House GOP Plan would have mixed results for the pharmaceutical industry.

The ACA reflected a complex bargain between the Obama administration and the pharmaceutical industry. The pharmaceutical industry benefitted from more insured people who could afford to purchase more drugs. It also benefitted from the closing of the "doughnut hole," the coverage gap between an initial threshold of drug costs that would be covered by Medicare Part D and a much higher catastrophic maximum after which Part D coverage would resume. The ACA eliminated that coverage gap. In return, the branded pharmaceutical industry agreed to a \$3 billion tax and cutbacks on Medicaid reimbursements for prescription drugs.

The House GOP Plan partially unwinds this bargain. The plan benefits the pharmaceutical industry by repealing the \$3 billion annual tax and maintaining the closure of the doughnut hole. Additionally, repealing the "medicine cabinet tax" may boost the sale of over-the-counter drugs. But the pharmaceutical

industry will lose to the extent that people no longer purchase prescription drugs because they lose their health insurance or are covered by plans that provide only limited coverage for expensive drugs, even while the ACA's cutbacks on Medicaid rebates are left intact.

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We will provide further updates as more details become clear regarding the Trump administration and Congress' plans for changing the ACA. Please do not hesitate to contact us with any questions.