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Primer: Understanding the Effect of the Supreme Court Ruling on the Patient Protection and Affordable Care Act

A staff paper prepared for BPC's Health Care Cost Containment Initiative

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ABOUT BPC

Founded in 2007 by former Senate Majority Leaders Howard Baker, Tom Daschle, Bob Dole and George Mitchell, the Bipartisan Policy Center (BPC) is a non-profit organization that drives principled solutions through rigorous analysis, reasoned negotiation and respectful dialogue. With projects in multiple issue areas, BPC combines politically balanced policymaking with strong, proactive advocacy and outreach.

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BPC's Health Care Cost Containment Initiative will produce a system-wide approach to cost containment that explores and evaluates the most promising value-based strategies that have the greatest potential for bipartisan support and political success in 2013. Through the Health Care Cost Containment Initiative, BPC has a unique opportunity to draw our four distinguished health and economic policy leaders – former Senate Majority Leaders Tom Daschle and Bill Frist, former Senator Pete Domenici and former Congressional Budget Office Director Dr. Alice Rivlin – together in a detailed set of discussions supported by quality analysis. Our goal in this endeavor is not to achieve a grand compromise, but rather to create a better substantive foundation for the ultimate political debate.

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CBO: SCOTUS Decision Projected to Save Federal Government $84 Billion, Leave Three Million More Uninsured

On July 24, 2012, it was a typical humid summer afternoon in Washington, D.C., when the Congressional Budget Office released an updated analysis of the Patient Protection and Affordable Care Act. The report reflected the Supreme Court's recent ruling to allow states to choose, rather than be required, to expand their Medicaid programs. For more details, see our previous post here.

Like the weather, the conclusion about the impact of the Supreme Court of the United States' (SCOTUS) ruling on the federal budget is a little dense and slightly foggy.

Background on the ACA Coverage Expansion

Starting in 2014, the Patient Protection and Affordable Care Act (ACA) will increase health insurance coverage among lower-income individuals in two ways: through an expansion of Medicaid, which will affect people who earn less than 138 percent[1] of the federal poverty level (FPL), and through federal subsidies to individuals who purchase commercial insurance plans through state- or federal-run insurance exchanges, which will affect people who earn between 100 and 400 percent of the FPL.

Medicaid. Prior to the Supreme Court's decision, the ACA required every state to enroll individuals earning up to 138 percent of the FPL at an "enhanced matching rate," meaning that the funding would largely be supplied by the federal government.[2] If a state chose not to expand Medicaid in this manner, it would forfeit the right to *all* federal funding for its Medicaid program—a punishment severe enough that every state was expected to undertake the expansion. As a result of the Court's decision, however, states may opt to expand or may decline to do so without any effect on their current federal funding, a decision that changes the Act's expected impact on coverage and federal budget outlays.

Because every state Medicaid program is different, each state's decision to expand, not to expand, or to partially expand produces a different impact on the federal government's responsibility to contribute to lower-income individuals' health insurance costs. For example, State X may currently offer Medicaid only to individuals whose income is below 75 percent of the FPL. So if State X chooses not to expand its program, the citizens between 75 and 138 percent of the FPL would not be eligible for Medicaid. Of course, the details vary by state and are often more complicated than simple FPL eligibility—sometimes eligibility depends on factors such as pregnancy or disability.

Insurance Exchanges. To address the unaffordability of insurance premiums in the individual and small-group markets, the ACA established health insurance exchanges that are designed to provide one-stop-shopping platforms in which consumers can compare and purchase insurance online. Offering consumers transparency in insurance pricing and

product information should help promote competition and affordability. The ACA also provides federal subsidies on a sliding scale to consumers between 100 and 400 percent of the FPL to help them purchase insurance through the exchanges. These subsidies, however, are not available for individuals with incomes under 100 percent of the FPL. Therefore, if some states forego the Medicaid expansion, many low-income people will be left without assistance—with incomes too high for Medicaid, but too low for subsidies to help purchase insurance on an exchange.

Effects on the Federal Budget and Coverage Expansion

Because the Supreme Court ruling made the Medicaid expansion optional for states, the Congressional Budget Office (CBO) anticipates that some states will in fact decline to expand and others will only undertake a portion of the expansion, leaving fewer Americans covered by Medicaid and thus reducing the projected spending of the federal government (as it would no longer have to contribute its matching share of Medicaid funding for those individuals). Although some of those uncovered people would then be eligible for exchange subsidies—at an added cost to the federal government—many will not qualify because their incomes fall below 100 percent of the FPL (i.e., the coverage gap described above). Accordingly, CBO projects that the decision to make the Medicaid expansion optional will reduce the federal deficit by $84 billion over the course of 11 years.

CBO and the Joint Committee on Taxation did not make predictions (as some were hoping they might) about which particular states will reject the Medicaid expansion. They did, however, project that in 2022, about six million fewer people will be covered by Medicaid as a result of some states deciding against expansion. The forecast estimates that roughly half of those individuals (three million) will instead receive subsidies through the exchanges, while the other half will remain uninsured.

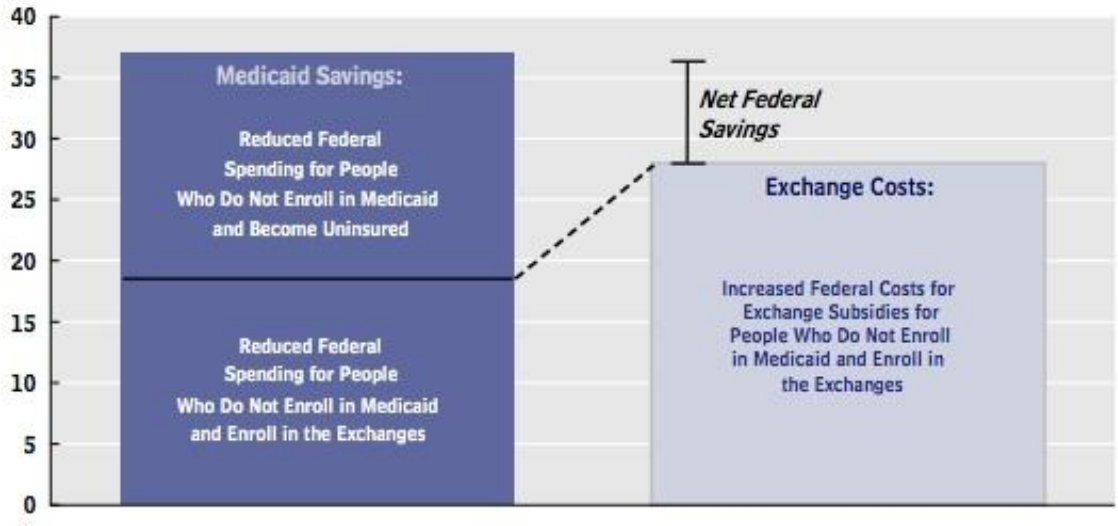
CBO's analysis also provides a useful rule of thumb for comparing (for the year 2022) the federal government's cost of enrolling someone in Medicaid versus its cost of subsidizing insurance purchases through an exchange (for a person earning between 100 and 138 percent of the FPL):

- Average federal cost of enrolling someone in Medicaid at the ACA-enhanced match rate = **$6,000**
- Average federal cost to subsidize someone earning between 100 and 138 percent of the FPL to purchase insurance on an exchange = **$9,000**

Figure 1.

Major Effects on the Federal Budget in 2022 of Changes in Medicaid Enrollment Due to the Recent Supreme Court Decision

(Billions of dollars)



Sources: Congressional Budget Office and the staff of the Joint Committee on Taxation.

So, although the cost to the federal government of covering individuals through exchange subsidies actually exceeds that of covering them through the expanded Medicaid program,[3] the federal government is expected to reap substantial savings, because half of the individuals who are ineligible for Medicaid are projected to remain uninsured (see figure above). Of course, there are other issues to consider when adding three million people back to the ranks of the uninsured, but from the perspective of the U.S. Treasury's balance sheet, the savings from each uninsured person is greater than the cost for each federally subsidized person in the exchange. Thus, the projected decrease in total federal spending on Medicaid ($289 billion from 2012–2022) is larger than the anticipated increase in total exchange subsidies ($210 billion over the same period).[4]

Why Some People Will Have Non-Medicaid Options and Some Will Not

In states that forego the expansion, most of the individuals earning less than the FPL who are not covered by the state's base Medicaid program will remain uninsured.[5] Moreover, as CBO explains, a lower percentage of those with incomes between 100 and 138 percent of the FPL will purchase private insurance, even with the subsidies, than would have joined Medicaid, due to higher out-of-pocket costs for premiums and cost-sharing. (This effect, however, would be partially offset by the opportunity to have better access to certain providers offered by private insurance through an exchange.)

Effects on the Insurance Exchanges

As a result of the Supreme Court decision, approximately three million additional individuals—primarily those between 100 and 138 percent of FPL—are now expected to enroll in the insurance exchanges. This influx of people may have a positive impact on the functioning of those exchanges. More consumers create more competition, and a competitive marketplace that makes insurance more affordable is one of the key principles underlying the insurance exchange concept.

CBO estimates, however, that premiums for insurance offered on the exchanges will be 2 percent higher than before the Court's ruling. This is due to the fact that the new enrollees, those with incomes between 100 and 138 percent of the FPL, will tend to have higher healthcare costs due to poorer health, and the ACA bars insurers from varying premiums on the basis of health status.

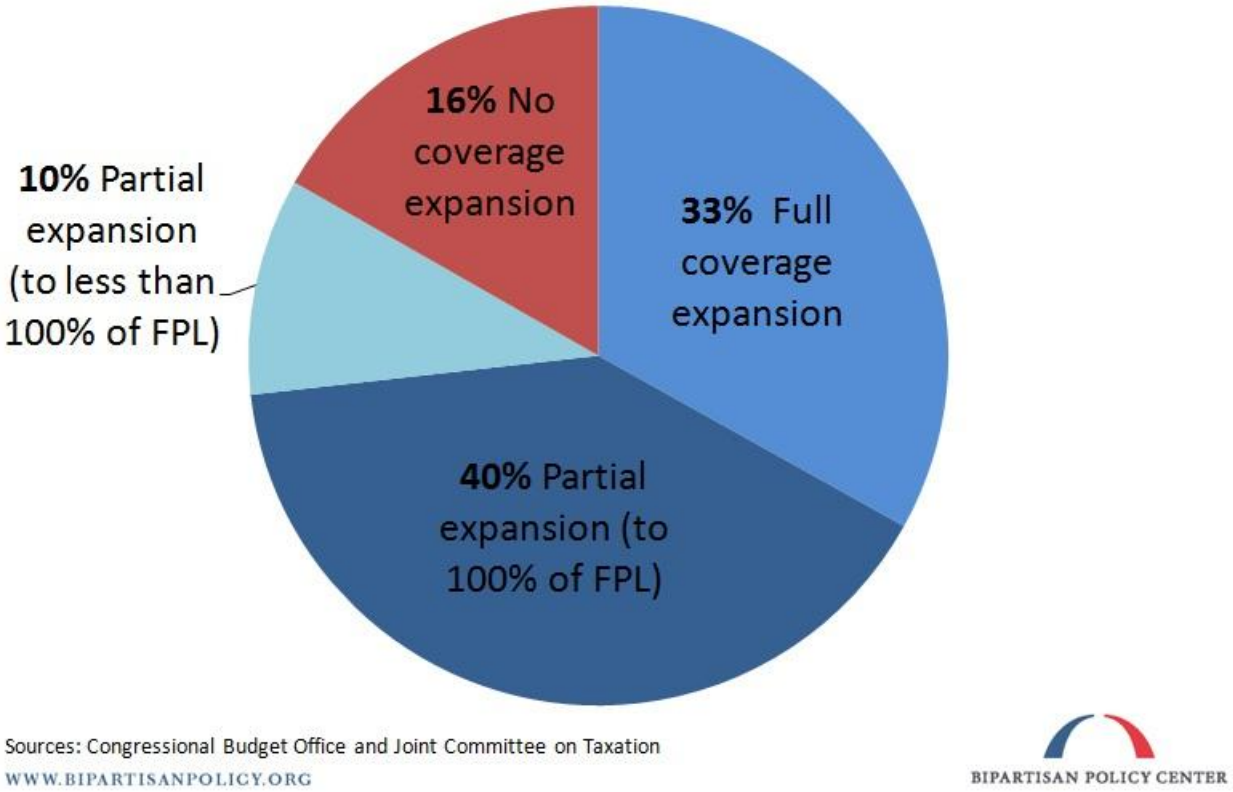
The influx of three million low-income enrollees into the insurance exchanges also increases the chance that the cap on the size of the total federal subsidies relative to gross domestic product will be triggered. The ACA calls for a downward adjustment to subsidy levels if premium and cost-sharing subsidies exceed a certain percentage of gross domestic product. If triggered, this adjustment could increase out-of-pocket costs for millions of individuals.

To Expand or Not to Expand

CBO does not predict specifically which states will forego the Medicaid expansion, but they do project that some will not expand at all, some will delay past 2014, and some will work out an arrangement with the Department of Health and Human Services to undertake a partial expansion. In particular, according to CBO, the Supreme Court ruling presents a strong incentive for states to seek an allowance to implement "a partial expansion of Medicaid eligibility to 100 percent of the FPL because, under the ACA, people below that threshold will not be eligible for subsidies in the insurance exchanges while people above that threshold will be if they do not have an offer of affordable coverage from an employer and meet other eligibility requirements." In other words, states may find it attractive to try to close the coverage gap by expanding Medicaid eligibility to 100 percent of the FPL but to go no further.

It is unclear, however, whether states will be allowed to partially expand Medicaid eligibility at the enhanced federal matching rates[6] or whether Section 1115 of the ACA provides the secretary of Health and Human Services the authority to allow a partial expansion as a "demonstration project." Additionally, Medicaid waivers are generally required to be budget neutral,[7] which could limit the ability of the federal government to allow partial expansions.[8]

Access to Medicaid in 2022 for Population that Was Scheduled to Receive Coverage under the ACA



The chart above depicts CBO's projected fate of the "newly eligible" or "expansion" population in 2022—that is, those individuals who would have gained access to Medicaid under the mandatory expansion. CBO estimates that one-sixth of the population who would have become newly eligible for Medicaid under the mandatory expansion resides in states that do not extend Medicaid coverage *at all*. For reference, according to data from the Urban Institute (reprinted in the chart below), more than one-sixth of the people who were projected to be newly eligible reside in Texas and Florida, both states that have indicated an intention to forego any expansion.[9]

Uninsured Adults with Incomes Below 138% of the FPL by Medicaid Eligibility Status, for the Nation and by State
(in thousands)

	Newly Eligible for Medicaid Under the ACA		Currently Eligible for Medicaid	Total Eligible Uninsured
	Less than 100% FPL	Less than 138% FPL	Less than 138% FPL	Less than 138% FPL
United States	**11,483**	**15,060**	**4,370**	**19,430**
Florida	995	1,295	257	1,552
Iowa	80	106	23	130
Louisiana	260	330	62	392
Mississippi	183	231	62	293
Missouri	267	351	51	402
Nebraska	56	78	21	99
Nevada	127	163	41	204
New Jersey	245	307	42	349
South Carolina	232	297	92	389
Texas	1,326	1,748	289	2,036

Key (based on analysis of available information from the Advisory Board Company):
Red = States that have indicated an intention to forego the Medicaid expansion
Green = States leaning toward foregoing the Medicaid expansion

Source: Urban Institute

Critical Questions Going Forward

A key question is whether states must meet all the conditions of the ACA Medicaid expansion to qualify for enhanced federal matching. If states are left with an all-or-nothing choice on expansion, they face a tough decision in the coming months. Despite the federal government paying 100 percent of the medical claims for the expanded Medicaid population in the first few years, some states remain concerned that the expansion will not be affordable, particularly over the long term. CBO recently estimated that if states expanded Medicaid eligibility as originally required under the ACA, their costs would increase by approximately $73 billion (or 7 percent of the expansion cost) between 2014 and 2022 (while the federal government's costs would increase by $931 billion, or 93 percent of the cost).

The projected increase in cost to states is a result of a number of factors, including: the "woodwork effect"[10]; additional personnel and process costs associated with expansion; and the portion of the costs for the newly expanded population to be covered by states, which scales up to 10 percent by 2020 and remains at that level indefinitely. Others may fear that

Congress, facing the need to reduce the deficit, will eventually scale back its contribution for this newly eligible population to lower than 90 percent.

Still, the Medicaid expansion is an opportunity for each state to provide insurance that is heavily subsidized by the federal government to many of its lowest-income citizens. Further, by closing the ranks of the uninsured, Medicaid expansion will reduce the uncompensated care costs that are burdening each state's hospitals, health professionals, and privately insured individuals.

If states are allowed to undertake a partial expansion at the enhanced match rates, the calculus changes. All states would face a strong financial incentive *not* to expand Medicaid coverage to persons earning above 100 percent of the FPL. With this decision, states could save money by choosing not to extend Medicaid to those earning between 100 and 138 percent of the FPL and limit the associated uncompensated care costs, as many of those individuals would buy insurance on an exchange with wholly federal subsidies. Moreover, individuals earning less than 138 percent of the FPL would have access to highly subsidized coverage. Of course, people who earn income in the 100 to 138 percent of FPL range would face increased out-of-pocket costs.

To expand or not to expand will remain a hotly debated topic in any event, but an allowance for partial expansion could greatly affect the outcomes. The updated estimates from CBO provide some insight into the possible budgetary effects of the Supreme Court ruling, but for now, the actual fate of the expansion remains unknown—a little dense and a little foggy.

Endnotes

[1] The income threshold is 133 percent of the FPL, but there is a 5 percent income disregard, making it effectively a 138 percent threshold.

[2] Medicaid is jointly financed by states and the federal government. To help make the Medicaid expansion more affordable for states, the federal government will foot the entire bill for the new beneficiaries through 2016. The government contribution will then gradually phase down to a 90 percent matching rate in 2020. These rates are much higher than the average historic Medicaid federal matching rate of 57 percent.

[3] Why does it cost the federal government more money to provide one individual with subsidies on the exchange than it does to provide him or her with Medicaid? There are two primary reasons: First, provider payments in Medicaid are generally far below rates in the rest of the market, and thus the coverage is provided to individuals at a lower cost. Second, in 2022, states would cover 10 percent of the cost for enrollees in the expanded Medicaid program, whereas the exchange subsidies are fully borne by the federal government.

[4] To be technically accurate, a very small portion of the projected $289 billion in reduced federal outlays derives from less spending on the Children's Health Insurance Program. Further, the $84 billion in savings over the 2012–2022 period incorporates the projection that there will be an additional $5 billion of deficit reduction from penalty payments relating to the individual mandate and other effects on tax revenue under the ACA.

[5] Additionally, Health and Human Services Secretary Kathleen Sebelius indicated that everyone earning less than 100 percent of the FPL will *not* have to pay the individual mandate penalty because they will qualify for a *hardship exemption.* See: U.S. Department of Health and Human Services (2012) Office of the Secretary: Letter to Governors. Washington, D.C., July 10.

[6] For more on skepticism over whether it is possible for states to partially expand Medicaid, see: Rosenbaum S and Westmoreland TM (2012) The Supreme Court's Surprising Decision on the Medicaid Expansion: How Will the Federal Government and States Proceed? *Health Affairs* 31(8): 1663–1672.

[7] For a more thorough discussion of this issue, see: Swendiman KS and Baumrucker EP (2012) Memorandum: Selected Issues Related to the Effect of *NFIB v. Sebelius* on the Medicaid Expansion Requirements in Section 2001 of the Affordable Care Act. Congressional Research Service, July 16, 7–10. Available at: http://www.healthreformgps.org/wp-content/uploads/crs-medicaid-update.pdf.

[8] For instance, if the Department of Health and Human Services allows a state to expand its Medicaid eligibility only up to 100 percent of the FPL, the federal government would be absolved from providing matching Medicaid funds for individuals earning between 100 and 138 percent of the FPL, thereby saving money, but instead it would have to cover the higher cost of providing subsidies for those that choose to purchase commercial insurance on an exchange. As mentioned in the text, CBO estimates that the cost to the federal government of subsidizing these low-income individuals' purchases of private insurance is roughly 50 percent more than the matching funds for their enrollment in Medicaid. Therefore, if more than approximately two-thirds of those who would have enrolled in the expanded Medicaid program purchase insurance on an exchange, the waiver would be budget-negative.

[9] Kenney GM, et al (2012) Opting Out of the Medicaid Expansion Under the ACA: How Many Uninsured Adults Would not Be Eligible for Medicaid? Urban Institute, July 5. Available at: http://www.urban.org/UploadedPDF/412607-Opting-Out-of-the-Medicaid-Expansion-Under-the-ACA.pdf.

[10] The "woodwork effect" occurs when people who are currently eligible for Medicaid "come out of the woodwork" to enroll after the expansion, prompted by increased media coverage, streamlined enrollment procedures, or the new requirement to obtain health insurance. Because these individuals are not considered newly eligible, they would be subject to the current (not the enhanced) federal-state match, increasing the financial burden on the states.