

# Tennessee's Option to Expand Medicaid Coverage: What Are the Issues?



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## INTRODUCTION

President Barack Obama signed the Patient Protection and Affordable Care Act (PPACA) in March 2010. Twenty-six states (not including Tennessee) plus various private organizations almost immediately filed suit in federal courts to block implementation. On June 28, 2012, the Supreme Court delivered a complex decision that will impact the delivery and financing of health care throughout the nation. The decision resolved constitutional challenges to two major provisions of PPACA – the individual mandate and the requirement that all states substantially expand Medicaid coverage or lose federal funding for Medicaid.

As described in previous articles in *Tennessee Medicine*,<sup>1,2</sup> the decision gave states the choice of whether to substantially expand Medicaid enrollment. In this report, we will attempt to give a glimpse of how complex and important that choice is and help, we hope, Tennessee make an informed decision. We will use data included in two previously published reports from our centers<sup>3,4</sup> to illustrate these challenges.

### What are the issues?

To understand the impact of the Court's decision, it is important to understand what the decision did and did not do. PPACA included several provisions specifically related to Medicaid. The most important provisions included expanding Medicaid eligibility to most nonelderly adults and

children ages six to 19 years with incomes through 138 percent of the federal poverty level (FPL), and increasing the Federal Matching Assistance Percentage (FMAP) rate for newly eligible Medicaid beneficiaries to 100 percent from 2014 to 2106 and then decreasing the rate gradually to 90 percent by 2020 and thereafter. Other Medicaid provisions that will impact the state include streamlining eligibility and enrollment systems; changing the method for determining income and eliminating asset tests; raising Medicaid payment rates for primary care providers to Medicare levels; and requiring states to maintain current eligibility requirements and benefits until insurance exchanges are implemented.

The law also stipulated that any state that did not implement the Medicaid expansion would lose all existing federal Medicaid matching, as well as the expanded funding that would be made available for the newly eligible. If Tennessee elected not to expand coverage to the PPACA limits, it would lose its current federal matching funds of approximately \$6.4 billion (in 2010), plus the estimated \$1 billion it would receive between 2014 and 2019 to cover the expanded population.<sup>4</sup>

### What did the Supreme Court do (and not do)?

The only provision related to Medicaid that was contested was the requirement for states to expand Medicaid eligibility to peo-

ple with incomes through 138 percent of the FPL. The Court held that this provision exceeded the power of Congress by "coercing the states to adopt the changes it wants." It concluded that the stipulation that any state that elects not to expand its Medicaid program would lose existing federal matching funds "is economic dragooning that leaves the States no real option but to acquiesce ..." and hence violates the Constitution.

Three parts of this ruling are especially important in understanding the impacts on Tennessee. First, the Court's ruling applied only to the provision requiring expansion of Medicaid eligibility to adults aged 19 to 64 years. The other Medicaid provisions were not overturned and thus remain in force as written, regardless of a state's choice about the Medicaid option.

Second, provisions not related to Medicaid that impact states are not affected by the Court decision. These include, among many others, the individual mandate with penalties for noncompliance; the establishment of insurance exchanges with federal subsidies; reducing both Medicare and Medicaid special payments for hospitals that serve a disproportionate share of indigent or uninsured patients (Disproportionate Share or DSH payments); penalties on certain employers who do not provide employee coverage; and numerous private insurance market reforms. These provisions that have substantial impacts on the

state are also not changed by the Supreme Court's ruling and will not be affected by the state's decision on Medicaid expansion. Finally, the Court ruled that the proposed expansion was legal as long as a state had the realistic option to not participate without losing its existing federal matching funds. Thus, states must have the option – but not the requirement – to expand Medicaid coverage as stipulated in the law without the threat of losing existing federal Medicaid funding.

### What is Tennessee's choice?

This ruling presents the critical challenge to every state, including Tennessee, of deciding whether to expand Medicaid coverage as stipulated in PPACA. On one hand, the availability of 100-percent federal financing through 2016 and at least 90-percent financing thereafter to expand services to a large and vulnerable population is a tempting incentive. However, the significant costs that remain with the state, as well as other important concerns, require states to undertake a careful analysis of their options.

### What factors influence the decision?

Many factors may influence the decision on expansion. These include estimating the projected number of new Medicaid enrollees and the effects expansion will have on their health and well-being; projecting the financial impacts to state and local governments as well as to healthcare providers in relation to their current fiscal conditions; and political and ideological concerns.

Unfortunately, none of these factors is simple. Many are state-specific, requiring a detailed analysis at the state level. For example, states that currently have greater Medicaid eligibility (e.g., Massachusetts projecting an increased Medicaid enrollment of less than 10 percent) will be affected less than other states with lower eligibility limits (e.g., Texas, projecting an increase of over 45 percent). States also vary widely in state fiscal resources, as well as specific characteristics of their delivery and financing systems. National estimates may thus be of little value in making this decision. And many of the factors will, as discussed later, be dependent on behav-

ioral choices made by individuals and businesses that are hard to predict with any degree of certainty.

### Who will be affected by the decision?

The group most directly affected by the state's decision includes the currently uninsured with incomes under 138 percent of the FPL who would become eligible under the Medicaid expansion provisions – the “expansion group.” We previously estimated that about 395,000 of the 910,000 uninsured in Tennessee had incomes of or less than 138 percent of the FPL and would be potentially eligible for TennCare under expanded eligibility.<sup>3</sup> Not all of these will actually enroll; we projected that about 225,000 previously uninsured people would realistically enroll.

Medicaid expansion is only one component of PPACA intended to reduce the number of uninsured in Tennessee.<sup>1,3</sup> Other major reforms that will increase coverage include expanding eligibility for young adults ages 19-26 years on their parents' private coverage, establishing insurance exchanges with premium subsidies, and various insurance market reforms.

If the state opts not to expand Medicaid, some of the expansion group will become insured through these alternate sources of coverage; that is, they would not remain uninsured. The Congressional Budget Office estimated that about two-thirds of these people will remain uninsured.<sup>5</sup> Thus, if Tennessee opts not to expand eligibility, we estimate that about 150,000 newly-eligible, now uninsured people who would have become insured under the expansion will remain uninsured.

### How will these people be affected?

Remaining uninsured will have important impacts on these Tennesseans. First, there is a well-known, clear and compelling relationship between a person's insurance and access to health care and their health status.<sup>6</sup>

Recent studies have further documented the positive impact of Medicaid expansion on the health of the previously uninsured. Benjamin Sommers and associates<sup>7</sup> compared health outcomes in three states that had significant Medicaid expan-

sions to others that did not. Medicaid expansion was associated with a 21-percent reduction in delayed care and a 6.1-percent reduction in adjusted all-cause mortality rates. One death was avoided for every 176 persons who gained insurance. Applying this result to Tennessee, the proposed Medicaid expansion will result in 853 fewer deaths per year among those in the expansion group.

In addition to health outcomes, expanded insurance coverage will have a positive impact on personal finances. Studies have also suggested that as many as 60 percent of personal bankruptcies are related to medical bills; 31 percent of persons filing for bankruptcy were uninsured at the time of filing and an additional 40 percent had been uninsured at some time during the prior two years.<sup>8</sup>

### How will the state budget be affected?

These gains come with costs. The greatest concern of states is the impact of Medicaid expansion on the state budget, especially at a time when states are already having difficulty funding their current Medicaid programs. For FY 2012, all states planned to implement at least one new policy to control Medicaid costs.

To understand the budgetary impacts of expansion, it is important to consider two groups of Tennesseans, in addition to the expansion group described earlier, who may now enroll in Medicaid. The first group includes people who are currently enrolled in private insurance and who now become eligible for Medicaid and switch from private coverage to Medicaid – that is, expanded public coverage would “crowd-out” private coverage. Although estimates of the size of this group vary widely, most analysts suggest only a relatively small proportion people with employer-sponsored coverage will choose Medicaid coverage.<sup>9</sup> Using a middle-level estimate, we calculated that TennCare expansion would lead to enrollment of 78,000 persons who were previously insured.<sup>3</sup>

The second group includes uninsured people who are currently eligible for Medicaid and are not currently enrolled but who will now enroll. This group is referred to as the “woodwork” or “welcome mat”

group. Incentives for new enrollment include the individual mandate, the simplified enrollment, and the increased public awareness of the importance of insurance. We estimated that in Tennessee, 14,000 previously eligible, uninsured people will now enroll.<sup>3</sup>

The total number of new Medicaid enrollees equals the sum of the new enrollees in the expansion group and the number in each of these two smaller groups. Thus, if the state opts to expand Medicaid under PPACA, we estimated that TennCare enrollment will increase by about 317,000, a 26-percent increase over current enrollment.<sup>3</sup> This number may be further modified by other factors in PPACA that will change eligibility based on current criteria, including the elimination of the asset test for eligibility and the changes in the method used to compute income.

The state's financial cost differs for these three groups of new enrollees. For the expansion and the crowd-out groups, the federal government will pay 100 percent of the costs through 2016. After that, the state will be responsible for up to 10 percent of their costs. Based on an annual increase in per-capita costs of 5.2 percent, the projected increase in enrollment would add \$315.5 million to the state budget between 2014 and 2019.<sup>4</sup>

For the woodwork group, the federal government will pay only a percent of the costs based on the current FMAP, that is, 66.36 percent. The state will be responsible for the remaining 33.64 percent of their costs. Using the same cost numbers as above, this group would add \$765 million to the state budget between 2014 and 2019; the total cost would thus be about \$1.08 billion.<sup>4</sup>

However, most of the woodwork group would enroll regardless of the state's decision concerning TennCare expansion. The net impact of increased enrollment directly affected by the state's decision to expand eligibility would be largely limited to the impact of the expansion and the crowd-out groups – \$315.5 million between 2014 and 2019 or 29 percent of the total cost of the increased enrollment. Thus, the major driver of the state costs of increasing TennCare enrollment – the woodwork group

– is independent of the state's decision on eligibility expansion.

There are additional, smaller costs to the state related to PPACA Medicaid provisions. These include: the increased administrative costs related to changes in enrollment procedures (of which as much as 100 percent will be paid by the federal government) and the larger number of beneficiaries; the required increase in TennCare payments to primary care providers to Medicare levels (currently, the national average Medicaid rate is 66 percent of Medicare rates) that are to be borne by the states beginning in 2015; and the possible reduction in federal payments as children currently enrolled in CHIP (with an enhanced FMAP of 76.45 percent) are transitioned into Medicaid (with an FMAP of 66.36 percent).

Medicaid expansion will also reduce other costs to states.<sup>10,11</sup> These include savings from transferring services that are currently fully or partially funded by the state to Medicaid with partial federal funding; that is, substituting federal funds for state funds. For example, many of the mental health and preventive services for the uninsured are paid for directly by states (currently, 44 percent of funds for states' mental health agencies are paid by local and state governments). With Medicaid expansion, much of these costs will be transferred to Medicaid and subject to substantial federal reimbursement, with a reduction in states' expenditures of between \$20 and \$40 billion.<sup>10</sup>

Expansion may also permit state and local governments to reduce direct payments for the care of the uninsured, with state savings of \$43-\$85 billion nationally by reducing the 30 percent of uncompensated care costs borne by state and local governments.<sup>10</sup> Some states may also save by transitioning certain current beneficiaries, such as those eligible for less than the full basket of Medicaid services, to the category of "newly eligible" with full federal funding. States may also reduce Medicaid enrollment of certain groups with incomes over 138 percent of FPL who are currently eligible, such as the "medically needy" and pregnant women, and who may be transitioned to subsidized coverage in the ex-

changes, with savings of \$21-\$28 billion. These enrollment and cost estimates are subject to wide fluctuations based on the assumptions that are used. Sommers and associates<sup>12</sup> projected a 10-million person range of new Medicaid enrollees nationally based on variations in take-up rates (45-80 percent), the proportion of newly eligible adults who switch from private to Medicaid coverage (15-60 percent), and the percentage of previously eligible adults who enroll (20-50 percent). In addition, it is not clear whether the healthcare costs for the new enrollees will be less than that of current enrollees (with projections as low as 60 percent) because they are on average in better health, or if costs will be greater because of pent-up demand for care and adverse selection. These significant variations in predictions render the financial evidence on which to make an informed decision highly speculative and uncertain.

The net effect of Medicaid expansion on the state budget will be the balance between these costs and the savings. Nationally, the Urban Institute has estimated that states will save between \$41 and \$132 billion between 2014 and 2019.<sup>10</sup> The bottom line will vary from state to state.

Several states have commissioned complex and complete financial analyses including these and other factors. These estimates have shown a wide variation in results, from significant savings to significant costs. Each state will need to determine the relative impacts of the costs and savings on its finances and population based on its own particular circumstances. Many of these studies have included costs unrelated to the Medicaid expansion option, such as the high costs of the woodwork group, and have not included various options for savings.<sup>11</sup> Thus, a careful reading of existing assessments and a thorough analysis of all fiscal consequences in future evaluations are needed to make a true evidence-based decision.

### How will the healthcare delivery system be affected?

The expansion decision will also have consequences to every part of Tennessee's healthcare system. Physicians, hospitals

and other healthcare providers will be affected by the impact of Medicaid expansion on uncompensated care. We estimated that in 2010, the uncompensated care load in Tennessee provided by hospitals, physicians and other community providers was about \$4.1 billion. Full implementation of PPACA provisions, including the Medicaid expansion, would reduce this by \$2.3 billion.<sup>3</sup> If Tennessee opted not to expand Medicaid eligibility, this reduction in uncompensated care would fall by an estimated 27 percent or \$610 million per year. The loss of revenue generated by the reduction in uncompensated care is significant for hospitals. Hospitals face substantial drops in revenue from several sources. Among these is the scheduled sharp reduction in Medicaid and Medicare disproportionate share (DSH) funds that remain part of PPACA. Under remaining provisions of PPACA, Medicaid DSH is scheduled to be reduced by 50 percent and Medicare DSH by 25 percent, beginning in 2014. The added revenue from Medicaid expansion was projected to compensate for these losses; without expansion, hospitals – especially safety net hospitals that received much of the DSH allotments – will be hard pressed to compensate for these losses without cutting services.

### How will the decision affect the overall economy of Tennessee?

The decision to expand or not to expand TennCare eligibility will also impact the overall economy of the state. Expansion is projected to generate over \$1 billion in new funds flowing into Tennessee from the federal government between 2014 and 2019.<sup>4</sup> These new monies will increase revenues for healthcare providers who will, in turn, purchase goods and services from all sectors of the state's economy. Every new dollar flowing into the state generates about \$2.60 in overall economic value to the state, creates jobs, and generates additional tax revenues for the state. FMAP payments for the some 150,000 people who would stand to gain Medicaid coverage under the eligibility expansion option would generate about \$2.9 billion in economic value to Tennessee between 2014 and 2019 and create about 7,950 jobs in

2019. Opting not to expand coverage would, in turn, result in the loss of these added values.

A final positive impact of Medicaid expansion on the state's economy will be the macroeconomic gains that come from better population health resulting from expanded insurance coverage.<sup>13</sup> As shown by international comparisons and historical studies, improved health in a community can be expected to increase worker productivity, enhance local and external investment, and free public funds used for caring for the ill to be used for other community needs, such as schools and other infrastructure needs.

### What other issues are at stake?

Opting out of Medicaid expansion will also uncover several problems that are the unintended consequences of eliminating only one part of a complex law. One substantial impact relates to the provision for federal subsidies to purchase private coverage in exchanges for persons with incomes of 100 percent to 400 percent of FPL. Those with incomes under 100 percent are not eligible for subsidies, based on the assumption at the time the law was passed that they would be eligible for Medicaid and, hence, not be in need of subsidies. However, if a state opts not to expand coverage, these people will have incomes too high to be eligible for Medicaid and too low to receive subsidies, creating a “donut hole” in coverage.

### What other concerns do states have?

Certainly, philosophical and political issues will also impact the decision. These include positions of state leaders on the relative role of state and federal governments in determining policy and issues of political party alliances. Of course, the largest political issue will be the outcome of the November 2012 elections, at both the federal and state levels.

Other concerns relate to the difficulty in backing off from expansions in the future if conditions require. Governors and others have also expressed concerns about the future of federal commitments as the federal government itself faces substantial budgetary and political pressures. Once expansion is implemented, states will find it

politically (and humanistically) difficult to reduce eligibility, as prior TennCare experience illustrates.

This brief overview has, we hope, provided a hint of the complexity of the decision facing the leadership of Tennessee. It is a choice that will affect the health of a large number of Tennessee residents and the financial well-being of virtually all parts of the state's healthcare enterprise and its general economy. It is also a decision fraught with financial and political uncertainties. Careful and thoughtful analysis combined with wisdom will be needed to do the right thing. +

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