INDUSTRY PANEL DISCUSSION
Hosted by Alvarez & Marsal

THE AFFORDABLE CARE ACT
CHANGING THE BUSINESS OF HEALTHCARE

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Although the central goal of the 2010 Patient Protection and Affordable Care Act (ACA) is to significantly reduce the number of uninsured Americans by providing affordable healthcare coverage options through Medicaid and new Health Insurance Exchanges or Marketplaces, there continue to be a growing number of concerns surrounding the impact on patient care, program costs and allocation of capital in the future.

Leading professional services firm Alvarez & Marsal (A&M) recently convened a group of top healthcare industry experts to address key provisions of the ACA and identify the challenges and opportunities ahead for healthcare owners, operators and investors.

During A&M’s 8th Annual Healthcare Industry Leadership Conference, sponsored by The Deal, speakers addressed the implications of an expanding dual-eligible population, defined as those Americans who are eligible for both Medicare and Medicaid. The ACA has enabled the states and the federal Centers for Medicare and Medicaid Services (CMS) to find more efficient and integrated mechanisms for providing care to 9.6 million dual-eligibles.

States have been spending the bulk of their Medicaid dollars on the disabled and elderly. “So, 75% of the folks covered under Medicaid have been moms and kids, but they represented only 31% of the costs. Now with the dual expansion, you have 9% of the enrollees being elderly, 16% being disabled, and those two groups are using up 69% of the Medicaid costs,” said Ed Griese, Managing Director at Alvarez & Marsal.

States can propose demonstration projects that would test new models aligning healthcare financing and/or delivery, such as capitated care or managed fee-for-service. At present, 26 states have submitted plans to CMS to develop such demonstration projects. Ian Adler, Senior Managing Director of Healthcare for Marwood Group, said New York is starting a dual eligible pilot program, called FIDA, in July 2014. “From a premium perspective, these health plans are going to be looking at something like $8 billion just in the demo.”

That’s a lot of money for the insurers, but it’s also a big gamble. Long-term care is expensive and hasn’t been proved to work under capitation, he said.

It’s a big step for providers because they grandfather current nursing home residents away from the dual eligible program, but all new nursing home residents will now be in managed care plans. Adler adds that starting next July instead of getting paid by New York State, these nursing homes will be paid by AmeriGroup, Aetna, or another insurer. “It’s just going to turn the industry
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around,” Adler noted, and there’s a question whether it will be successful.

Thomas Scully, General Partner at Welsh, Carson, Anderson & Stowe, said, “It’s great for healthcare businesses. You may not like the policy, but it’s hard not to like the investment impact on healthcare businesses. The floodgates are opening up,” he noted, “The ACA is worth $100 billion in 2014. It’s worth $200 billion by 2016.”

For those states that opt to expand Medicaid, the federal government picks up 100% of the cost of the expansion for the first three years, 2014 through 2016. The federal portion tapers down in subsequent years, to 90% by 2020.

Tony Keck, Director of Health and Human Services for South Carolina Governor Nikki Haley, explained that South Carolina has decided not to take the federal expansion of Medicaid. “Right now we have 731,000 people who are uninsured, a little over 1 million in Medicaid. The private market has about 2.4 million people.” Keck noted that with no expansion, there will be 433,000 people eligible for exchange subsidies, about a 71 percent decrease in the number of uninsured in the state.

Keck points out how hospitals look at the way things are changing in terms of shifting revenue streams. “Unfortunately, they’re not doing very good modeling,” adds Keck, “we need to go from a revenue-generating model to one where people are focused on cost avoidance. When I look at some of the states’ hospitals’ bottom lines, I become more convinced that it’s not necessarily the state’s job to pay for all of that,” adding that it may be the state’s job to pay for some. “But that’s where the real struggle is right now,” Keck said.

“One thing that’s been interesting to me over the last three years, as you have seen the market reacting to ACA implementation and realizing what’s on the horizon is, we have seen a lot of hospital consolidation,” Eric Zimmerman, Partner with McDermott Will & Emery, commented.

Adler said, “In certain regions they’re very organized and they have good politics and good advocates but to get from A to B, to go from serving 24 million to 58 million, I think that’s going to be a huge task, especially since these all have to be not-for-profits. There can’t be any private capital in them,” Adler noted.

“Hospitals are high-tech office buildings that house doctors. Doctors drive care,” Scully explained. “I think we’re going through another big cycle of hospitals buying up lots and lots of docs. It’s not going to work. There’s never been a hospital in the country that’s bought docs and that’s worked in the long run, that I’ve ever seen. It’s going to unravel in the next 10 years. Docs are going to get smarter and they’re going to get more educated and there’s going to be another round of physician practice rollups.”

However, Zimmerman said, “Hospitals must at least be involved if not be the center of that dynamic because they’re the only ones with the capital, they’re the
only ones with the information technology systems that are essential to being able to manage care in these ways."

Hospitals must grow and get stronger on a local market basis, said Guy Sansone, Managing Director and Head of Healthcare for Alvarez & Marsal. "As simple as it sounds to talk about organic growth, and investing in your existing infrastructure and your existing business, you have to position yourself or your business model or whatever you’re going to do in an ACO to deal with compliance issues."

"You have to deal with continued growth, shrinking margins, investment in plants, investment in technology, and if you want to grow by acquisitions, find ways to allocate all the capital," Sansone said. "At the same point in time, you must understand where your balance sheet stands and what you can do there."

"A lot of factors go into this, and as basic as the concept of free cash flow is, having a plan, understanding you have to move on it as opportunities jump is really something that you’re going to hear a lot of talk about in the next three to five years," Sansone noted.

Certainly M&A is one way to allocate capital, Sansone noted. "The game is changing here and it’s changing pretty quickly. How do corporations view the world now, going forward, in terms of how they’re going to allocate capital?"

"The dilemma that a lot of folks have on asset allocation is they believe they know what they need to spend money on over the next five years, but I don’t think anybody knows what they need to spend money on," said Keith Pitts, Vice Chairman at Vanguard Health Systems.

"There’s also the short-term, long-term balance. So you have this dilemma: how do you balance out keeping everybody happy on the investor side and how do you run the company in the long-term?" he asked.

"The healthcare industry is going through radical changes, changes that are driven so much by macroeconomic and broad-based policy decisions," Sansone noted. "Organizations are trying to see how to strategically position themselves both in their own communities and whether or not they have to affiliate or partner with other organizations That plus the fact that most of these organizations have capital structures that were designed three, four, five years ago under a different world. You’ve got lots of change both strategic operationally and from a balance perspective that are all coming together at the same time."

Sansone added, “The implementation of the Affordable Care Act has not been a turning point per se. It’s been a wake-up call that things are going to be different. Some of those things have started to be different and some of these things are going to be different. Most organizations are grappling with how to best prepare.”