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It's Joe Manchin's World, We're Just Living in It: Forecasting the Healthcare Outlook

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Sen. Joe Manchin's (D-WV) announcement yesterday that he cannot support the Build Back Better (BBB) reconciliation package as currently constructed almost certainly represents a death knell for the $1.6 trillion package. We cannot account for the timing of Sen. Manchin's decision, though we note that every politician's first, second, and third instinct is self-preservation, and Sen. Manchin clearly has decided that playing the spoiler is good for his political health. He is probably correct considering that Donald Trump won West Virginia by 39 percentage points in 2020.

If we give Sen. Manchin the benefit of the doubt, he likely was spooked by the twin reports last week from the Bureau of Labor Statistics (BLS) and the Congressional Budget Office (CBO). The former announced that inflation rose in November at a rate faster than any time since 1982 and the latter reported in response to an inquiry from Republicans that the BBB would add $3 trillion to the deficit if all the spending priorities were made permanent.

Next Steps: A Salvage Operation & Regular Order

We expect that President Biden, Speaker of the House Nancy Pelosi (D-CA), and Senate Majority Leader Chuck Schumer (D-NY) will attempt in the coming weeks to rescue their floundering agenda. Realistically, there likely are only two pathways forward for Democrats and the policies espoused in the House-passed BBB: (1) passage of a substantially scaled down (e.g., < $1 trillion in spending) *and* budget neutral reconciliation bill in 1Q22 or (2) passage through regular order (i.e., with 60 votes in the Senate) as part of whatever spending package Democrats can negotiate with Republicans before the current Continuing Resolution (CR) expires on February 18.

From a healthcare perspective, since nearly all the spending priorities in the BBB are partisan in nature, their only hope for survival is if Democrats can cobble together a skinny BBB (we think the odds are less than 50 percent). The relatively good news for Democrats is that since most of the major healthcare offsets in the BBB have the support of Sen. Manchin, it may be possible for a smaller reconciliation package to still contain as much as **$270 - $300 billion** in healthcare spending priorities, though the actual number likely would be far less and include only one or two policies. In the absence of a reconciliation bill, we do not believe that any of the major healthcare spending priorities in the BBB can survive, though some of the more modest policies may be able to generate some Republican support.

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Healthcare Priorities in a Theoretical Skinny BBB

Any skinny BBB will very likely need to be truly budget neutral to secure the support of Sen. Manchin, meaning all spending must be fully offset. We believe that Sen. Manchin is in favor of the biggest healthcare offsets that collectively generate over $270 billion in savings over 10 years, per the CBO as we highlight in our November 22 report.

- ✓ **Repeal of the Rebate Rule ($142.6 Billion)**: While this policy is gimmickry at its finest, Sen. Manchin supported a similar policy in the Bipartisan Infrastructure Framework (BIF), meaning we assume he would be on board with this offset.

- ✓ **Drug Price Negotiation ($78.8 Billion)**: Sen. Manchin is supportive of Medicare negotiating drug prices, including the BBB's compromise approach that limits negotiation to a subset of mature, expensive branded products without generic or biosimilar competition.

- ✓ **Inflation Caps in Medicare (~$41.7 Billion)**: The CBO scored the BBB's inflation cap policy that applies to Medicare and the commercial market as saving $83.6 billion, about one-half of which is due to its application to Medicare. We do not believe that the Senate Parliamentarian will find that the application to the commercial market complies with the Byrd Rule.

- ✓ **Part D Redesign ($1.5 Billion)**: This policy has broad support across both parties. It is likely the only drug pricing policy that could theoretically clear Congress under regular order, though we doubt that Democrats would allow it to move without the other drug pricing reforms opposed by Republicans.

- ✓ **Non-Expansion State Penalties (~$30 Billion)**: The Senate had already jettisoned a 12.5 percent cut in non-expansion state Medicaid DSH allotments included in the House-passed BBB prior to Sen. Manchin's announcement, but there is another policy in the bill that would prevent non-expansion states from receiving federal funding through an uncompensated care waiver program for any expenditures applicable to the expansion population, effective beginning in 2023. This policy targets Florida, Kansas, Tennessee, and Texas, each of which currently receive federal funding for uncompensated care pools through 1115 Waivers, with Texas accounting for the vast majority of the spending. While the CBO scored the two policies in concert as saving $34.5 billion, we believe that the latter policy generates the preponderance of those savings. Since West Virginia is an expansion state, it is theoretically possible that Sen. Manchin could support this policy.

- ✓ **Medicaid & CHIP Policies ($4.6 billion)**: Requiring states to provide 12 months of continuous Medicaid coverage to eligible children and permanently authorizing the Children's Health Insurance Program (CHIP) collectively save $4.6 billion by reducing

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"churn" and offering less expensive coverage versus alternative sources, respectively. We believe that Sen. Manchin likely would support these policies because they generate savings.

In aggregate, the healthcare offsets that we believe Sen. Manchin supports generate about $300 billion in savings. Even if the non-expansion state penalties were jettisoned for being too punitive, the collective healthcare savings from repealing the Rebate Rule, making drug pricing reforms, and the applicable Medicaid and CHIP policies are nearly $270 billion. As such, a skinny BBB could potentially include up to $270 - $300 billion in healthcare spending.

Identifying Spending Priorities

The House-passed BBB contains nearly $410 billion in healthcare spending, meaning that any skinny BBB would have to remove at least one-fourth of such spending, and likely much more. We believe that the only hope Democrats have for salvaging a reconciliation bill is to eliminate most of the budgetary gimmickry opposed by Sen. Manchin, meaning that all spending programs likely will have to be authorized for the full 10-year budget window, or something very close to that period. As such, it likely would be possible for Democrats to incorporate only a couple of healthcare spending priorities into a smaller reconciliation bill. Below we discuss which of the major BBB healthcare policies is most and least likely to be included in a skinny bill, in descending order.

- ✓ **Extending the Enhanced ACA Exchange Tax Credits**: The House-passed BBB extends the expanded tax credits through 2025 at a cost of $73.9 billion, but making these subsidies permanent would cost $220 billion, per the CBO. Despite the high cost, we believe that this is the most likely healthcare spending program to be included in a smaller reconciliation bill because the policy is very popular across the Democratic Caucus. Additionally, this is the only healthcare policy in the BBB that extends an existing program, meaning if Democrats take no action that individuals will lose a current benefit. Extending the benefit for the full 10 years would crowd out nearly all other healthcare spending, but we believe this policy likely must be the Democrats' top priority.

- ✓ **Addressing the Medicaid Gap**: The House-passed BBB would allow low-income individuals to access essentially free Exchange coverage through 2025 at a cost of $57 billion, though making these subsidies permanent would cost $180 billion. This policy is a top priority for Sen. Raphael Warnock (D-GA), the most endangered Senate Democrat in 2022. While we believe this policy is the second most-likely to be included in a skinny reconciliation bill, it may fall victim to cost constraints and it very likely will have to compete with the enhanced home and community-based services (HCBS) initiative (see below).

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- ✓ **Enhancing HCBS for Disabled & Elderly Medicaid Enrollees**: Establishing a 6-percentage point plus-up in the federal match for states that enhance HCBS in Medicaid costs $149.6 billion. This policy is a top priority for disability advocates and the home care industry; however, we tend to believe that this policy would end up being cut from a skinny BBB. It is possible that it could beat out the Medicaid Gap policy for the second (and likely last) healthcare seat in a reconciliation bill because it costs less over a 10-year budget window and therefore can be more easily shoehorned into a smaller bill, but we believe the Medicaid Gap initiative is more likely to prevail for political reasons.

- ✓ **Insulin Cost-Sharing Caps**: The House-passed BBB spends $6 billion to cap OOP spending insulin in the Medicare and commercial markets. While it is quite possible that the cost-sharing limit as it applies to Medicare ($900 million) could be included in a skinny reconciliation bill because it is relatively inexpensive and politically popular, we do not believe that the application to the commercial market ($5.1 billion) complies with the Byrd Rule. However, it is at least theoretically possible that a commercial cap could pass through regular order since many Republicans support such a policy.

- ✓ **Other Medicaid Policies**: The House-passed BBB contains several additional Medicaid policies, including increasing the federal match for the expansion population from 90 percent to 93 percent in 2023 – 2025, making permanent an enhanced cap and federal match for the Territories, phasing down the 6.2-percentage point enhanced match put into effect at the outset of the Covid-19 public health emergency (PHE) to avoid a spending cliff when the PHE designation expires, phasing-in the redetermination process when the PHE expires to prevent a coverage cliff, creating a 3.1-percentage point penalty for states that establish more stringent coverage requirements after the PHE expires, expanding Medicare and Medicaid coverage of CDC-approved vaccines, and requiring states to provide 12-months of post-partum coverage to qualifying pregnant women up from 60-days under current law. Most of these policies are likely now dead, though we do believe there is a chance that the policies related to phasing-down the 6.2-percentage point enhanced match and phasing-in the redetermination process in Medicaid could potentially be addressed through regular order to prevent extreme disruption to state Medicaid programs upon the eventual expiration of the PHE.

- ✓ **Hearing Benefit in FFS Medicare**: This new benefit, which costs $36.7 billion, was already nearly dead because of Sen. Manchin's strong opposition. We see no plausible pathway forward for this or any other Medicare expansion policies in a scaled back reconciliation bill.

- ✓ **Public Health Spending**: The House-passed BBB contains $46.6 billion in spending for public health programs, healthcare workforce training, and certain policies designed to improve staffing at skilled nursing facilities (SNFs). Our expectation is that these policies would almost certainly be excluded from a skinny BBB.

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More Uncertainty Than Certainty

The unknowns far exceed the knowns currently, but we do expect the President, Speaker Pelosi, and Senator Schumer to continue to work towards a pathway for some skinnier version of reconciliation legislation. The existing reconciliation authority technically lasts until September 30, 2022, though practically speaking, Democrats have until roughly mid-March before the election season will fully overtake any legislative efforts. And realistically, February 18 is probably the true deadline for action since that is the expiration of the current CR and therefore represents the last, best hard deadline for action.

We think there is probably less than a 50 percent chance that Democrats can salvage the BBB in a skinny form. However, because Sen. Manchin is supportive of most of the large healthcare offsets in the BBB, it is theoretically possible that up to $300 billion in healthcare spending could be included such a bill. Our expectation is that the true total healthcare spending probably would be markedly less and likely could incorporate only a couple of the spending priorities from the House-passed BBB.

Our expectation is that extending the expanded ACA Exchange tax credits is the highest priority for Democrats to prevent middle class individuals from losing a current benefit. The only other healthcare policies that likely could be included in a skinny BBB are an insulin OOP cap in Medicare and either a policy addressing the Medicaid Gap or enhancing HCBS in Medicaid, and we believe the former is better positioned than the latter.

Administrative Actions

Should legislative efforts fail, we believe that the Biden Administration will pivot to taking administrative actions on healthcare policies, including drug pricing reforms. We assume that the Administration would pursue those policies elucidated in President Biden's drug pricing plan, which we discuss in our September 9 report. Our expectation is that the Administration would focus most immediately on Part B drugs rather than Part D because the former is practically and politically easier to tackle. We also think they will likely address issues that are less aggressive but more likely to be implemented to avoid the pitfalls of the prior two administrations. Some ideas included in the President's plan that could be addressed in a demonstration project include outcomes-based pricing, shared savings, and bundled payments in Part B to incentivize the uptake of less expensive alternatives such as biosimilars; reduced or capped OOP spending for seniors in Part D taking expensive medicines, $0 cost-sharing in the Part D Low-Income Subsidy (LIS) program, or passing through direct and indirect remuneration (DIR) to the point of sale in Part D; or establishing Part B + D global payments for prescribers of expensive medications treating certain high-cost diseases (e.g., Hepatitis C, HIV/AIDS, opioid use disorder, and diabetes) to drive utilization towards less expensive alternatives.

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We note that the recently published Fall 2021 Unified Agenda includes a vague reference to a proposed rule entitled, "Alternative Payment Model," which is described as a rule that "would propose a new mandatory Medicare payment model under [the Centers for Medicare and Medicaid Innovation]. This model would test ways to further our goals of reducing Medicare expenditures while preserving or enhancing the quality of care furnished to beneficiaries." The description could describe almost anything and may very well be a placeholder that the Biden Administration will fill once it has more clarity on what can or cannot be accomplished legislatively. The proposed rule is projected to be published in August 2022, though we note that the dates included in the Unified Agenda are largely just guesstimates. In theory, though, such a model could be operational beginning in 2023, absent practical, political, or legal delays.

Final Thoughts

Sen. Manchin's announcement yesterday represents a huge setback for President Biden and Congressional Democrats. The only remaining option is to try and salvage a skinny BBB that caters to Sen. Manchin's demands for less spending, full offsets, and less budgetary gimmickry. We are not sanguine Democrats can prove successful, but there are still several weeks before the opportunity is likely closed for good.

The only silver lining for Democrats as it relates to healthcare is that Sen. Manchin embraces the major healthcare offsets in the BBB, meaning there may be room for some meaningful healthcare spending in a skinny BBB. As such, we believe that the drug pricing reforms in the House-passed BBB are still alive (for now) and that they could fund certain policies that are beneficial to managed care organizations with exposure to the Exchange market and to providers.

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