



THE SECRETARY OF HEALTH AND HUMAN SERVICES  
WASHINGTON, D.C. 20201

December 10, 2012

Dear Governor:

As we implement the Affordable Care Act, I want to take this opportunity to provide you with an update on how some important provisions of the health reform law apply to the territories. Over the past several months, my staff has appreciated the opportunity to meet with several governors of the territories and participate on calls with their staffs to discuss this issue.

The Department of Health and Human Services (HHS) and our colleagues at the Internal Revenue Service and the Department of the Treasury have received a number of questions from territories specifically about the applicability of provisions related to the Affordable Insurance Exchanges (Exchanges). After a careful review of the law, we want to share the following information that we hope will be helpful as you determine whether to establish an Exchange or enhance your Medicaid program.

The enclosed document provides additional details regarding the standards for an Exchange established by a territory. My department remains committed to providing technical assistance to territories, and I encourage your staff to continue working with our Centers for Medicare & Medicaid Services as you think through Exchange implementation and enhancements to your Medicaid program.

As you know, the Affordable Care Act provided \$1 billion for territories to provide financial support through an Exchange or to increase the funding for their Medicaid programs. The enclosed document provides a description of how we intend to allocate this funding to the territories.

I appreciate your partnership as we strive to provide all our nation's citizens with access to affordable, quality health care. I look forward to our continuing work together as we implement these important improvements to our health care system.

Sincerely,

Kathleen Sebelius

Enclosure

## Information for the Territories Regarding the Affordable Care Act

### *Background*

The territories are important partners in the implementation of the Affordable Care Act. HHS clarified in a July 29, 2010 letter to the territories that the insurance market reforms (including the essential health benefits) in the Public Health Service Act, as amended by the Affordable Care Act, apply to territories because the definition of “state” in the Public Health Service Act<sup>1</sup> includes territories.<sup>2</sup>

Other provisions of title I of the Affordable Care Act that are not incorporated into the Public Health Service Act rely on the definition of “state”<sup>3</sup> as “the 50 States and the District of Columbia.” Section 1323 of the Affordable Care Act establishes the territories’ ability to establish Exchanges and provides that a territory that elects to establish an Exchange will be “treated as a state” for the purposes of the Exchange standards in sections 1311 through 1313 of the Affordable Care Act.<sup>4</sup> We note that the following provisions fall outside of those sections, and therefore are not applicable to territories: the Consumer Operated and Oriented Plan program, the Basic Health Program, the waiver for state innovation, and the Multi-State Plan Program implemented by the U.S. Office of Personnel Management.

Under section 1323, a territory that establishes an Exchange will be allocated funding to provide premium assistance and cost-sharing assistance to residents who obtain health insurance through the territory’s Exchange. Territories determine how these assistance payments are made, provided that there are no gaps in assistance between the income level at which an individual would be eligible for Medicaid and the income level at which an individual would be eligible for Exchange premium and cost-sharing assistance. Additionally, the premium and cost-sharing assistance provided must be consistent with the agreement between the territory and the Secretary of HHS directed by section 1323(b)(2). If a territory does not elect to establish an Exchange, the funding allocation for the territory’s Medicaid program will be increased to the amount allocated to the territory under section 1323 in the form of federal Medicaid matching funds during the time period between 2014 and 2019.

On January 20, 2011, HHS issued a solicitation (also referred to as a Funding Opportunity Announcement) publicizing the availability of the first round of funding for cooperative agreements. Territories can use these funds for a variety of Exchange implementation activities including background research and initial stakeholder consultation. As indicated in the funding announcement, if a Territory is awarded grant funds and subsequently does not meet the section 1323(a)(1) requirement to establish an Exchange, those grants funds will be subject to all applicable grant regulations and policies, including 45 C.F.R. section 92.52.

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<sup>1</sup> Section 2791(d)(14) of the Public Health Service Act.

<sup>2</sup> Section 1101 of the Social Security Act defines “state” as “except where otherwise provided, includes the District of Columbia and the Commonwealth of Puerto Rico, and when used in titles IV, V, VII, XI, XIX, and XXI includes the Virgin Islands and Guam. . . . Such term when used in titles XIX and XXI also includes the Northern Mariana Islands and American Samoa.”

<sup>3</sup> Section 1304(d) of the Affordable Care Act.

<sup>4</sup> Specifically, the territory would be treated as a state for the purposes of part 2 of subtitle D of the Affordable Care Act, which includes sections 1311 through 1313.

### *Territory Exchange Establishment and Operational Standards*

The Affordable Care Act directs a territory that elects to establish an Exchange to do so consistent with section 1321 of the Affordable Care Act, provided that such election is received by HHS no later than October 1, 2013. HHS has established an Exchange approval process based on a state's completion of an Exchange Blueprint,<sup>5</sup> which directs states to demonstrate its operational readiness to operate an Exchange and compliance with the relevant regulations. A territory must complete and adhere to the relevant components of the Exchange Blueprint to receive approval of its Exchange. We received inquiries regarding the extent to which territories could obtain exemptions from any provisions associated with Exchange establishment and operation. HHS is open to working with territories to explore options for implementing Exchange standards in a way that makes sense for a territory's unique market.

In order for an Exchange to gain approval by HHS, the territory must comply with the standards in sections 1311 through 1313 of the Affordable Care Act, and the implementing regulations that outline minimum Exchange functions, minimum qualified health plan certification standards, enrollment periods, self-sustainability, and financial integrity. Although the term "qualified health plan" (QHP) is defined in a different section<sup>6</sup> of the Affordable Care Act, the standards for QHPs apply to plans offered through Exchanges established by the territories because those standards are the basis for many of the provisions in sections 1311 through 1313. As such, health insurance products offered through a territory's Exchange must comply with all provisions governing QHPs.

The temporary risk corridors program established in accordance with section 1342 of the Affordable Care Act may be implemented by the Federal government in territories approved to operate an Exchange because it includes issuers of QHPs.

Furthermore, because the initial open enrollment period begins October 1, 2013, it is both the formal date by which a territory must elect to establish an Exchange and the date by which the Exchange must be sufficiently operational to conduct open enrollment for coverage beginning January 1, 2014. Territories will not be able to elect to establish an Exchange after October 1, 2013.

If a territory establishes an approved Exchange, it may elect to establish a transitional reinsurance program or a risk adjustment program (or both) consistent with the provisions in sections 1341 and 1343 of the Affordable Care Act, respectively. A territory wishing to operate a risk adjustment or a reinsurance programs would be subject to the regulations HHS promulgates to implement these sections including 45 CFR 153.100 and 153.110, which, as proposed, direct a State to publish a notice of benefit and payment parameters in certain circumstances if it wishes to operate a risk adjustment program or a reinsurance program. HHS will not establish a reinsurance program or a risk adjustment program on behalf of a territory should the territory elect not to establish these programs. We note that a territory is not prohibited from establishing its own reinsurance or risk adjustment program pursuant to its own law. Such a program would not be established under the authority in sections 1341 and 1343, and thus would not be subject the standards established by HHS for operation of these programs.

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<sup>5</sup> Exchange Blueprint published May 16, 2012: <http://cciiio.cms.gov/resources/files/Exchangeblueprint05162012.pdf>.

<sup>6</sup> Section 1301(a) of the Affordable Care Act.

In order to operate a transitional reinsurance program in 2014, a territory must notify HHS of its intention to do so by March 1, 2013, so that HHS can work with the territory to ensure sufficient contributions are collected to fund reinsurance payments. The territory would also operate the program in accordance with the standards set forth in proposed 45 CFR 153.200-250.

In order to operate a risk adjustment program in 2015 and later, pursuant to proposed revisions to 45 CFR 153.310, a territory would obtain HHS approval to do so. We note that HHS would not operate risk adjustment in a territory if the territory was not approved to operate the program for the benefit year. For 2014, we request that a territory notify HHS of its intent to operate a risk adjustment program by March 1, 2013. For benefit year 2015 and later, pursuant to 45 CFR 153.310(a)(4), a territory would need to be approved to operate the program prior to March 1 of the year prior to the applicable benefit year. A territory could use any federally certified methodology to operate their risk adjustment program, or could submit an alternate methodology, pursuant to 45 CFR 153.330. Such a submission, and subsequent HHS certification of the alternate methodology, must be made in accordance with the standards set forth at 45 CFR 153.330.

### *Exchange-related Tax Provisions*

As described above, territories wishing to establish an Exchange must comply with the applicable<sup>7</sup> Exchange standards and the implementing regulations. However, the analysis is somewhat different with respect to three Exchange-related tax provisions that were also enacted under the Affordable Care Act:

- The premium tax credit under section 36B of the Internal Revenue Code of 1986 (the Code) enacted as section 1401 of the Affordable Care Act.
- The minimum coverage provision of section 5000A of the Code enacted as section 1501 of the Affordable Care Act.
- The employer responsibility provision of section 4980H of the Code enacted as section 1513 of the Affordable Care Act.

The territories have their own tax laws and therefore they generally determine how those tax laws apply. We can, though, offer the following observations after consultation with the Department of the Treasury.

Non-mirror Territories: In a territory that has a distinct tax code rather than a tax code that mirrors the federal Code, in general, the provisions in the federal Code referenced above do not impose obligations or confer benefits upon residents of the territory unless the territory chooses to enact a comparable provision. For example, the premium tax credit under section 36B of the Code would generally not apply in a territory that has its own distinct tax code. The territory, however, could choose to enact a comparable credit under its own tax code to implement the premium assistance required by section 1323 of the Affordable Care Act.

The minimum coverage provision implemented through section 5000A of the federal Code also would not apply in a territory that has its own distinct tax code because there is an explicit exemption for residents of the territories provided by operation of section 5000A(f)(4)(B).<sup>8</sup> The

<sup>7</sup> Requirements in part 2 of subtitle D of the Affordable Care Act.

<sup>8</sup> Section 5000A(f)(4)(B) provides that each bona fide resident of a U.S. possession is treated as having minimum essential coverage for each month in which the individual resides in the U.S. possession.

territory could, however, choose to enact a comparable provision under its own law for similar policy reasons that underlie the minimum coverage provision.

Finally, the employer responsibility provision (federal Code § 4980H) generally would not apply in a territory that has its own distinct tax code; as with the other provisions, the territory could choose to enact a comparable provision under its own law.

Following from this understanding of how the Exchange-related tax provisions do not apply in the non-mirror code territories, we believe that a territory that elects to establish an Exchange in which the premium tax credit of section 36B was not in effect would not have to comply with Exchange standards related to advance payments of the premium tax credit and cost-sharing reductions. Rather, the section 1323 agreement between such territory and HHS regarding the use of the appropriated funds would address how premium assistance is provided to territory residents, meaning that the territory's Exchange could have a mechanism for the provision of financial assistance that is different than the tax credit under section 36B of the federal Code.

Mirror Territories: In a territory that has a mirrored tax code,<sup>9</sup> it appears that the premium tax credit under section 36B of the federal Code does not violate general mirroring principles based on our discussions with the Treasury. Therefore, it seems likely that section 36B of the federal Code would be mirrored into the territory's tax code to provide premium assistance to bona fide residents of the territory who enroll in health coverage through the territory's Exchange and meet eligibility requirements that mirror those set forth in section 36B of the federal Code.<sup>10</sup>

A territory that elects to establish an Exchange, and in which section 36B of the Code is mirrored, must comply with the applicable Exchange standards related to advance payments of the premium tax credit and cost-sharing reductions. We note that if section 36B is mirrored into the territory's tax code, the tax credit will offset the territory's tax revenues, a cost that will be partially offset by the appropriation in section 1323 of the Affordable Care Act, described below. In such territories, section 1323 also requires an agreement between the territory and HHS regarding the use of the appropriated funds; we anticipate that this agreement would address how premium assistance provided through this mechanism is structured in order to eliminate any gap in assistance for individuals between the income level at which the territory provides Medicaid assistance and the income level at which premium assistance is provided.

The minimum coverage provision of section 5000A of the federal Code, however, provides an explicit exemption for residents of the territories by operation of section 5000A(f)(4)(B). It is our understanding that the territories with mirror codes generally are not obligated to mirror federal Code provisions that explicitly address treatment of residents of the territories.

Furthermore, it appears that the employer responsibility provision of section 4980H of the federal Code would not apply in a territory with a mirror code because it is categorized as an excise tax in the federal Code. It is our understanding that the territories with mirror codes generally are not obligated to mirror excise tax provisions. Each territory with a mirror code,

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<sup>9</sup> That is, a tax code with income tax provisions that are generally identical to those in the federal Code except for the substitution of the name of the relevant territory for the term "United States" where applicable.

<sup>10</sup> In the main, section 36B of the federal Code appears generally compatible with a mirror code system. When mirroring section 36B, however, a territory may need to modify its application with respect to any differences in the way a territory shares information between HHS, the Exchange and its tax administration for the delivery of advance payments of the premium credits and cost-sharing assistance to individuals under a mirrored section 36B(f).

however, must undertake its own analysis of whether these sections of the federal Code would be mirrored in the territory's own tax code.

If a provision comparable to section 5000A(a) of the federal Code was not applicable under a territory's law, the territory would not have to comply with related provisions such as section 1311(d)(4)(H) and (d)(4)(I) of the Affordable Care Act, which relate to certification of exemptions for the minimum coverage provision.

Since territories (even those with mirror codes) would provide premium assistance under the territory's law and not under section 36B of the Code, section 1402 of the Affordable Care Act, the requirement to provide cost-sharing reductions, is inapplicable to residents of territories who purchase qualified health plan coverage through a territory Exchange. We note that a territory Exchange can adopt similar cost-sharing reduction eligibility criteria and administrative requirements as those required by section 1402.

#### *Territories Electing Not to Establish an Exchange*

If a territory elects not to establish an Exchange, HHS will not operate a Federally-facilitated Exchange in that territory. Territories are not eligible for a State Partnership Exchange with HHS, since the State Partnership options are variations of a Federally-facilitated Exchange. Further, a territory will not be able to enter into a regional Exchange with states that have a Federally-facilitated Exchange, including a State Partnership Exchange.

Instead, section 1323 of the Affordable Care Act directs that a territory that does not elect to establish an Exchange will receive an increase in the dollar limitation that applies to federal funds for the territory's Medicaid program.

#### *Allocation of Funding*

As noted above, the Affordable Care Act provides a total of \$1 billion for the territories to use, beginning in 2014 and through 2019, for (1) the premium and cost-sharing assistance in an HHS-approved territory Exchange or (2) an increase in the dollar limitation applicable to the territory under section 1108(f) and (g) of the Social Security Act (the Act) to fund the territory's Medicaid Program. The allocation for Puerto Rico is specified under the statute as \$925 million.<sup>11</sup> Below is a description of how we intend to allocate the remainder of the amount appropriation under section 1323 of the Affordable Care Act.

For other territories, the Affordable Care Act<sup>12</sup> provides \$75 million of the \$1 billion appropriation to be allocated as specified by the Secretary. We intend to allocate the \$75 million among these territories using the same allocation basis as provided under section 1108(g)(5) of the Act as amended by Affordable Care Act. The allocation will be based on the proportion of the amounts of the jurisdictions' section 1108 limitations on funding applicable to the jurisdictions on March 30, 2010 (the date of enactment of section 1108(g)(5) of the Act as amended by Affordable Care Act). The following chart shows the calculation of the jurisdictions' allocation of the \$75 million in accordance with this provision:

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<sup>11</sup> Section 1323(c)(2)(A) of Affordable Care Act.

<sup>12</sup> Section 1323(c)(2)(B) of Affordable Care Act.

ALLOCATION OF \$75 MILLION UNDER SECTION 1323 OF ACA			
A	B	C	D
Jurisdiction	FY 2010 Sec 1108 Cap Including ARRA Increase	Percent of Total	Allocation Under Section 1323 of ACA Col C x
		Col B/Tot. Col B	\$75,000,000
American Samoa	\$12,051,000	22.01%	\$16,510,330
Guam	\$17,836,000	32.58%	\$24,436,001
Northern Mariana Islands	\$6,656,000	12.16%	\$9,118,974
Virgin Islands	\$18,200,000	33.25%	\$24,934,695
Total	\$54,743,000	100.00%	\$75,000,000
*Total allocation of \$75 million available for period 1/1/2014 - 12/31/2019			

Under section 1323(c)(1) of the Affordable Care Act, the funds allocated are available for the purposes indicated above during the period January 1, 2014, and ending December 31, 2019.

#### *Applicability of Medicaid-related Eligibility Provisions*

The Affordable Care Act amended certain provisions of the Medicaid statute that apply generally to the territories. Section 1902(a)(10)(A)(i)(VIII) of the Act authorizes coverage under the Medicaid program for the new group of non-pregnant individuals aged 19 through 64 with household income no more than 133 percent of the federal poverty level (FPL) beginning January 1, 2014. The regular federal medical assistance percentage (FMAP) matching rate applicable for territorial medical assistance expenditures (55 percent) is applicable for the medical assistance expenditures associated with this new group. The increased FMAP specified in section 1905(y) of the Act for expenditures for “newly eligible” individuals in this new group is only available under the statute for the 50 states and the District of Columbia and is not available for the territories.

Section 1902(a)(10)(A)(ii)(XX) of the Act, which authorizes optional Medicaid coverage for individuals under 65 years of age, not eligible for and enrolled in other Medicaid eligibility groups, and whose income exceeds 133 percent of the FPL (but does not exceed the highest FPL income eligibility level under the state plan for the family size), also takes effect on January 1, 2014. This optional Medicaid expansion can be phased in based on categorical groups or income, as long as the State does not favor individuals with higher income over those with lower income. Parents can be enrolled in such an expansion only if their children are enrolled in some form of health coverage (either under the State plan, a waiver of the plan, or other health insurance coverage).

Under section 1905(b) of the Act, as amended by the Affordable Care Act, the regular FMAP for the territories increased from 50 percent to 55 percent effective July 1, 2011. The 55 percent FMAP for the territories will be applicable for both of the new Medicaid eligibility groups described above.

As provided in the final regulation, *Medicaid Program; Federal Funding for Medicaid Eligibility Determination and Enrollment Activities*, published in the *Federal Register* on April

19, 2011,<sup>13</sup> through December 31, 2015, the federal matching rate for the costs related to the design and development of mechanized eligibility determination systems is 90 percent, and the federal matching rate for the costs related to the continued operation of such systems is 75 percent. Furthermore, under section 1108(g)(4) of the Act, such costs are not applied against the territories' section 1108 caps.

The provision at section 1902(e)(14) of the Act, which directs states to use modified adjusted gross income (MAGI) for determining Medicaid eligibility for most non-elderly, non-disabled populations, will also apply to the territories as of January 1, 2014. MAGI-based income counting and household composition policies are described at 42 CFR 435.603 of a final rule<sup>14</sup> published March 23, 2012. This final rule also contained other changes that apply to the territories.

Each territory will continue to have the flexibility to use the national federal poverty level guidelines as applicable for the states and the District of Columbia, as published for each calendar year in the *Federal Register*, or to use different poverty guidelines by family size approved in the territory's Medicaid state plan based on cost of living. The FPL guidelines used by a territory will determine its actual income limit by family size for the adult group and other eligibility groups. For example, the dollar amounts by family size of 133 percent FPL for the adult group will vary according to the poverty guidelines in effect for a territory.

These changes will have limited effect on American Samoa and the Northern Mariana Islands in light of the waiver of most title XIX requirements granted to them under the authority of section 1902(j) of the Act.

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<sup>13</sup> The final rule was published at 76 Fed. Reg. 21950 (April 19, 2011).

<sup>14</sup> The final rule was published at 77 Fed. Reg. 17144 (March 23, 2012) and can be accessed at <http://www.gpo.gov/fdsys/pkg/FR-2012-03-23/pdf/2012-6560.pdf>.