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CLIENT ALERT

The Impact of Health Insurance Co-Op Liquidations on Providers

By Wendy G. Marcari and Jackie Selby

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A growing number of health insurance co-ops or "consumer operated and oriented plans" created under the Affordable Care Act ("ACA") are shutting down on their own initiative or on orders of state regulators because of their precarious financial condition. The failed co-ops include, among others, those in Colorado, Kentucky, Louisiana, Nevada, New York, and South Carolina, as well as one serving Iowa and Nebraska.

Nonprofit co-op insurers were intended to increase competition and provide less expensive coverage to consumers. However, low prices, lack of adequate government funding, restrictions on the use of federal loans for marketing, and low "risk corridor" payments from the Centers for Medicare & Medicaid Services ("CMS") created financial challenges for these insurance plans. Facing insolvency, state regulators have ordered many plans to cease offering coverage and be wound down.

There has been nationwide news coverage of these failures and the impact on consumers who lose their insurance coverage and must enroll in new plans, often at higher premiums. Taxpayers also suffer the consequences of co-ops that cannot repay the billions of dollars in loans given to them under the ACA.

Health care providers, such as hospitals and physicians (many of whom are already operating on thin margins) represent another category of victims of the insurance co-op failures. Providers' claims for medical services delivered to the insurers' members may not be paid in full. Time-consuming liquidation proceedings mean that the claims of providers will almost never be paid timely in accordance with applicable "prompt pay" laws.

The liquidation of health insurance co-ops is not dictated by federal bankruptcy law. Instead, the laws of the states in which the plans operate govern the process for the dissolution and distribution of assets.

In New York, for example, Article 74 of the New York Insurance Law authorizes the Superintendent of the Insurance Department, upon court order, to take control of, and liquidate, an insurer domiciled in New York. During the liquidation process, assets are marshaled and liquidated for cash. Claims against the insurer are submitted by creditors, reconciled, and adjudicated, if necessary, after which an equitable distribution is made to creditors.

The relative priority of claims and the order of distribution of the insurer's assets are also set forth in Article 74 of the New York Insurance Law. Claims under the insurance policies and claims by state and local governments for losses incurred are afforded "class two" priority, behind only the claims relating to the costs of the liquidation and administration. Claims designated in the junior classes include, among others, claims of the insurer's employees, claims of federal and state governments (other than claims for losses incurred), and claims of general creditors. Only after claims in each higher class are paid in full may holders in the next junior class receive a distribution. This statutory priority scheme evidences legislative intent to protect and prioritize the claims arising under the policy, such as the claims of providers. Other states have similar laws and priority schemes. Despite the high priority afforded to provider claims in an insurer's liquidation, however, distributions to providers are dependent upon the liquidation resulting in sufficient cash to pay such claims. Reserves are often inadequate.

Failure of Largest Health Insurance Co-Op Established Under ACA

In September 2015, the largest co-op established under the ACA, Health Republic Insurance Company of New York ("Health Republic"), was ordered shut down by New York State regulators. It was subsequently reported that a review of Health Republic's finances by the Department of Financial Services ("DFS") and CMS found that the insurer's financial condition is substantially worse than previously reported to DFS. State officials have advised that payments to providers may only be "modest." Prior to these announcements, providers were not privy to this information about Health Republic's financial condition. The providers may have been prohibited from stopping treatment of patients who had paid premiums to the insurer and from billing the patients for unpaid claims.

Complicating the issue in New York is the fact that Health Republic did not contract directly with the providers. Rather, it rented its provider network from another entity, MagnaCare. MagnaCare's provider agreements presumably did not obligate MagnaCare to pay claims not funded by Health Republic.

Losses suffered by providers on account of unpaid claims against the insurance co-op will have a significant impact on providers. According to a New York hospital trade group, Healthcare Association of New York State, Health Republic owes hospitals more than $160 million, excluding claims for care provided in November. To make matters worse, New York does not have a guaranty association that covers claims of health insurance companies, as some other states do.

As a result, many are calling for drastic changes. For example, the Greater New York Hospital Association ("GNYHA") is advocating for the establishment of a health insurance guarantee fund to protect consumers and providers in the event of a health insurer's insolvency or liquidation. Others are pushing for state funding and/or reform of the insurance rate approval process in order to set adequate insurance premiums.

Takeaways

Until a meaningful solution to the mounting economic challenges facing nonprofit insurance co-ops is implemented, more co-ops are likely to fail, leaving providers and other creditors holding the bag. Accordingly, to protect their interests, providers are encouraged to:

- submit their claims promptly and follow up on accounts receivable regularly,
- work collaboratively to advocate for needed financial support and reform in the industry, and
- consider including special protections in the agreements that they enter into with third parties when they become providers in those parties' networks.

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This Client Alert was authored by **Wendy G. Marcari** *and* **Jackie Selby.** *For additional information about the issues discussed in this Client Alert, please contact one of the authors or the Epstein Becker Green attorney who regularly handles your legal matters.*

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