

Takeaways From The High Court's Medicare Ruling

By **Michael Kimberly and Ethan Townsend**

On Monday, the U.S. Supreme Court decided *Azar v. Allina Health Services, et al.*,^[1] an important case affecting all hospitals that provide care to the millions of Americans who are eligible for Medicare. The court held that the government's inclusion of Medicare Part C enrollees in the calculation of the "Medicare fraction" for fiscal year 2012 was unlawful and should be vacated.

The court's decision not only changes the standards for Medicare reimbursements to hospitals for serving low-income patients for fiscal year 2012, but it also has potentially far-reaching implications for the government's ability to change Medicare policy.

The Hospitals' Claim

The case involved a challenge to the U.S. Department of Health and Human Services' calculation of "Medicare fractions," a key determination in calculating reimbursements that hospitals are entitled to receive for caring for low-income patients under Medicare Part A.

Since 2004, the government has sought to include Medicare Part C patients in the denominator for the Medicare fraction, which measures the proportion of a hospital's Medicare patient population that is low income. A higher proportion leads to greater reimbursements. Including Part C patients in the denominator of the Medicare fraction lowers the proportion and therefore lowers reimbursements to hospitals that serve low-income patients.

The government promulgated a final rule in 2004 requiring the inclusion of Part C patients, but that rule was vacated by a federal district court on procedural grounds. The government cured the procedural defects of the rule in 2013, but the 2013 rule applied prospectively only. Shortly thereafter, the government nevertheless published 2012 Medicare fractions that included the Part C patients in the relevant calculations.

A group of hospitals challenged the government's inclusion of Part C patients for pre-2013 reimbursements, arguing that it violated Section 1395hh(a)(2) of the Medicare Act. That provision requires the government to provide public notice of, and an opportunity to comment on, any "rule, requirement or other statement of policy ... that establishes or changes a substantive legal standard governing ... the payment for services."

The district court sided with the government, holding that the government was not required to use Section 1395hh(a)(2)'s notice-and-comment procedures before including Part C patients in the 2012 Medicare fraction calculation. In an opinion by then Judge Brett Kavanaugh, the U.S. Court of Appeals for the D.C. Circuit reversed, concluding that Section 1395hh(a)(2) required the government to use notice-and-comment procedures and that the 2012 Medicare fraction calculations were therefore unlawful.

The Supreme Court's Decision

In a 7-1 decision by Justice Neil Gorsuch, the Supreme Court affirmed the invalidation of the



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rule. At bottom, the question presented was whether the agency's determination that Medicare Part C patients should be included in the Medicare fraction represented a change in a "substantive legal standard" within the meaning of Section 1395hh(a)(2). If it did represent such a change, then notice-and-comment procedures were required under the Medicare Act.

The court held that the inclusion of Part C patients in the Medicare fraction was "substantive." It held in particular that "substantive legal standard" under Section 1395hh(a)(2) means any legal standard or determination that creates rights and obligations, distinguishing "substantive" in this sense from "procedural."

The court thus expressly rejected the government's attempted analogy to the Administrative Procedure Act, which differentiates not between "substantive" rules and "procedural" rules, but between "substantive" rules and "interpretative" rules. The court did not mince words on this score, holding that the Medicare Act "pretty clearly" does not use the word "substantive in the same way the APA does."

For one, the Medicare Act provides that "statements of policy" can establish a change in a substantive legal standard. Under the APA, by contrast, statements of policy are necessarily interpretive rather than substantive.

Similarly, the Medicare Act expressly permits retroactive substantive changes to be made by interpretative rules and statements of policy. As the court explained, "this statutory authority would make no sense if the Medicare Act used the term 'substantive' as the APA does" because the APA prohibits those mechanisms for making retroactive substantive changes.

The court also noted that, elsewhere in the Medicare Act, Congress expressly elected to incorporate particular APA provisions, including when to exempt the government from notice-and-comment obligations. But Congress did not cross-reference the relevant provisions of the APA when establishing the affirmative notice-and-comment requirements under the Medicare Act. This disparate inclusion and exclusion, the court said, must be understood as deliberate.

Finally, the court rejected the government's legislative-history and policy-based arguments. In the court's view, the legislative history could be read either way, and there was insufficient evidence that imposing notice-and-comment procedures would meaningfully affect the government's administration of Medicare. The court thus concluded that when the government changes or establishes a substantive legal right, as opposed to a procedural right, when implementing the Medicare Act, it must use the notice-and-comment procedures as required under Section 1395hh(a)(2).

Key Takeaways

The court's decision in this case has significant and obvious implications for 2012 Medicare fraction calculations, and — in turn — reimbursements for services provided in fiscal year 2012.

More broadly — and although the decision will not have an impact on reimbursements for fiscal year 2013 or beyond — the case has substantial implications for the government's ability to change substantive policies under the Medicare Act without first observing the act's notice-and-comment requirements. If a change is properly characterized as substantive rather than procedural, the public will be entitled to a notice of the proposed

change and an opportunity to participate in the policymaking process. The decision thus guarantees greater agency transparency. It also affords the agency additional opportunities to avoid errors and make better informed decisions. Hospitals and other members of the regulated public should keep an eye out for substantive changes in Medicare policy not made according to such procedures.

The court's opinion is also notable for its strong rejection of legislative history and atextual policy arguments, continuing the court's march to a more strictly textualist approach to statutory interpretation.

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[1] Azar v. Allina Health Services, et al., No. 17-1484