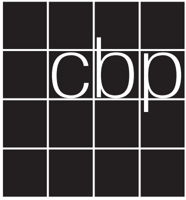

CALIFORNIA BUDGET PROJECT

budget brief

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PRESIDENT OBAMA'S PROPOSED FRAMEWORK FOR MEDICAID WOULD SHIFT COSTS TO CALIFORNIA

Driven by an impending deadline to avoid a default on the national debt, President Barack Obama has proposed a $4 trillion deficit reduction package that includes substantial reductions to core programs over the next decade. The Obama Administration's proposal includes cutting federal Medicaid spending by $100 billion over 10 years, primarily by shifting a larger share of Medicaid costs to the states. The proposed federal cuts would further undermine California's Medicaid Program, Medi-Cal, at a time when the state is struggling to maintain services. Faced with reductions to federal funding, California would be forced to scale back Medi-Cal coverage for 7.4 million individuals, reduce payments to health care providers, or increase state spending. These reductions would also significantly impede California's ability to ensure health coverage, one of the core goals of the recent federal health reform law. This *Budget Brief* examines how the Administration's proposal would impact California's Medi-Cal Program.

What Does the Administration Propose for Medicaid?

At the center of the debate is President Obama's "Framework for Shared Prosperity and Shared Fiscal Responsibility," which the Administration released in April as a basis for deliberations for reducing the federal budget deficit. Within this framework, the Administration proposes to reduce spending, including cutting federal Medicaid costs by $100 billion over 10 years by making significant changes to the program. Proposed changes to Medicaid include:

- **Calculating a single "blended" rate for Medicaid matching funds.** Under current law, the federal government matches state dollars using different formulas for different groups of individuals and some specific services. The framework introduced by the President in April would replace these rates with a single "blended rate" that would apply to all Medi-Cal expenditures.[1] Given that this proposal was released in the context of reducing federal spending, the blended rate would provide California with less federal funding for Medi-Cal than would be provided by the various matching rates that are currently in effect.
- **Restricting states' ability to use special taxes paid by health care providers to draw down federal matching funds.** To increase their ability to access federal Medicaid funds, nearly all states – including California – impose taxes on health care providers' revenues to generate additional state dollars that are used to draw down federal funds.[2] The Administration's framework would reduce the maximum allowable provider tax by an unspecified amount, thereby reducing the amount of revenues states can raise.[3]

A "Blended Rate" Would Reduce Federal Matching Funds for Medi-Cal

The Administration proposes to establish a single "blended" matching rate for each state, replacing the multiple federal

What Is Medi-Cal?

Medi-Cal is California's version of Medicaid, a federal-state program that provides health coverage to 7.4 million low-income Californians. Medi-Cal covers nearly one out of five Californians. In 2010-11, California spent an estimated $12.8 billion for Medi-Cal, or 13.8 percent of General Fund spending. The state and federal government generally share in the cost of the Medi-Cal Program, with the federal government paying 50 percent of most Medi-Cal costs and California paying the other half.

In order to receive federal funding, the federal government requires states to provide coverage to specific groups, such as children whose parents have incomes below the federal poverty line, families receiving cash assistance, and seniors or persons with disabilities who receive Supplemental Security Income/State Supplementary Payment (SSI/SSP) grants.[4] States may also cover individuals beyond the federally mandated populations. Medi-Cal, for instance, provides health coverage to pregnant women between 134 and 200 percent of the federal poverty line, seniors and persons with disabilities with incomes above SSI/SSP grant levels, and other low-income individuals.

Federal law also requires states to provide a core set of benefits, such as doctor visits, hospital care, nursing home care, and laboratory services. California offers additional services, such as coverage for prescription drugs, family planning, and durable medical equipment.[5]

matching rates in the Medicaid Program. To help the federal government achieve savings, the new blended rate would be set at a level that provides states with less federal funding than under current law. Experts identify two problems with this approach:

- **First, the proposed blended rate would shift the growing costs of Medicaid to states without constraining the costs of the program.** The Administration's proposal is designed to achieve a specified level of savings, rather than to change the underlying structure of the Medicaid Program, with the goal of reducing costs. By changing the formula used to determine the level of funding a state would receive, rather than identifying ways to improve the efficiency of Medicaid, the shift to a blended rate would simply shift costs from the federal government to states at a time when cash-strapped states are ill-prepared to take on additional responsibilities.[6]

- **Second, determining a fair blended rate would be extremely difficult.** In order to calculate a state's blended rate, federal officials would be required to make a number of complex assumptions, in some instances with little historical information to use as a starting point. While the Administration has not made a specific proposal for how the calculation would be made, the process would likely require calculation of a rate based on what a state would receive under current law – taking into account the rate for various population groups and services – and then adjusting that rate downward in order to achieve the targeted level of savings.[7] This would be complex and subject to considerable error since the calculation would require assumptions regarding the number of people who would be likely to enroll in Medicaid as well as the services that they may use. To the extent that the federal government underestimated the number of people who would become eligible for Medicaid under the Affordable Care Act of 2010 (ACA) or the cost of the services they would use, a state's cut under the Administration's framework would be disproportionately large.

Significant Cuts in Medi-Cal Funds Could Undermine the Health Care Reform Law

The Administration's framework would cut spending at a time when states are planning for the expansion of Medicaid coverage included in the ACA. Deep cuts in federal funding would break the promise made to states as part of the ACA, which is that the federal government would pay the full cost of those newly eligible for coverage for three years, thus providing an important incentive for states to aggressively enroll these individuals in health coverage. The federal share of cost will decrease modestly in subsequent years until the federal matching rate is fixed at 90 percent for 2020 and beyond. The generous federal funding under the ACA means that California could draw down nearly $30 in federal funds for each state dollar it invests in Medi-Cal coverage for newly eligible adults between 2014 and 2019.[8]

Under the framework, the generous federal matching rate for adults who are newly eligible in Medi-Cal would be "blended" with other federal rates and subsequently lowered. The reduction in federal funds would shift the cost of insuring newly eligible adults to California at a time when the state can ill-afford to support additional costs. As a result, California could choose to implement the health care reform law less aggressively in order to hold down its own costs. Consequently, many Californians who otherwise would have obtained Medi-Cal coverage due to the ACA would remain uninsured.

Reducing Provider Taxes Could Lead to Medi-Cal Cuts

In addition to their general purpose dollars, states raise revenues to support their Medicaid programs by imposing taxes on providers. These taxes are imposed, often with the support of health care providers, because they allow states to receive additional federal matching funds. These funds are then used to maintain services and payments to providers. In 2010-11, for example, health care provider taxes generated $2.5 billion that California used to match an equivalent amount of federal funds.[9] These funds were used to increase payments to providers and fund children's health services in Medi-Cal and the Healthy Families Program.

The Administration's framework proposes to limit states' ability to use these levies by gradually reducing the maximum allowable provider tax rate. The Congressional Budget Office noted that "an argument against [restricting provider taxes] is that lower federal payments could shift more of the burden of the Medicaid Program's growing costs to the states and possibly provide an incentive for states to scale back their spending …. Unless states were willing to pay more of the costs themselves …, access to health services for low-income people might be diminished."[10]

Conclusion

President Obama and Congressional leaders are considering various means of reducing the nation's deficit, including reductions to the Medicaid Program. The Administration's proposal would do little to constrain the Medicaid Program's costs, but would, instead, shift costs to states at a time when many are facing sizable budget shortfalls. A reduction in federal support would, for example, force California to increase state spending or reduce services available to the 7.4 million individuals who depend on Medi-Cal for their health coverage.

Who Is Affected By Medi-Cal Cuts?

President Barack Obama's "Framework for Shared Prosperity and Shared Fiscal Responsibility" aims to reduce the federal deficit, in part, by cutting Medicaid costs by $100 billion over 10 years. The President's proposal would significantly reduce the amount of federal funding California receives for Medi-Cal. To compensate for lost federal funding, California would either need to spend more to maintain current services or make substantial reductions to Medi-Cal.

Federal cuts to Medi-Cal would follow years of reductions imposed by California to cut costs in Medi-Cal. Since 2008-09, the state has made $2.9 billion in cuts to Medi-Cal, including reducing benefits for adults with Medi-Cal coverage and requiring individuals to pay more. Additional reductions to Medi-Cal could further erode services for 7.4 million Californians, including:

- **Persons with disabilities.** Persons with disabilities make up 12 percent of those enrolled in Medi-Cal, yet account for 36 percent of the program's costs.[11] Medi-Cal currently pays for doctor or clinic office visits, durable medical equipment, and long-term care, among other costs.
- **Seniors.** Seniors make up 13 percent of individuals enrolled in Medi-Cal, yet account for 26 percent of the program's costs.[12] Medi-Cal pays for two-thirds of nursing home care in California.[13]
- **Children.** Children make up about half of the Medi-Cal population. Any reduction in funds could disproportionately affect children because they make up the largest share of those covered.
- **Pregnant women.** Medi-Cal paid for 41.3 percent of births in California in 2006, the most recent year for which data are available.

Hanh Kim Quach and Jean Ross prepared this Budget Brief. *The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. General operating support for the CBP is provided by foundation grants, subscriptions, and individual contributions. Please visit the CBP's website at www.cbp.org.*

ENDNOTES

[1] The President's proposal would also include funds for the Children's Health Insurance Program – Healthy Families in California – in the new blended rate. Office of the Press Secretary, *Fact Sheet: The President's Framework for Shared Prosperity and Shared Fiscal Responsibility* (The White House: April 13, 2011). Federal funds pay 65 percent of the cost of the Healthy Families Program.

[2] The maximum allowable provider tax rate is scheduled to increase from 5.5 percent to 6 percent of gross revenues after September 30, 2011. Congressional Budget Office, *Budget Options Volume I: Health Care* (December 2008), p. 137.

[3] President Obama's proposed budget for federal fiscal year 2012, released in February, proposed to gradually reduce the maximum allowable tax on providers between 2015 and 2017. US Department of Health and Human Services, *HHS Budget in Brief,* downloaded from http://www.hhs.gov/about/FY2012budget/fy2012bib.pdf on July 12, 2011.

[4] In addition, state Medicaid programs must provide coverage to pregnant women and children under age 6 in families with incomes at or below 133 percent of the federal poverty line, some seniors with Medicare coverage, and certain other individuals.

[5] In recent years, the Legislature has cut several Medi-Cal benefits, including adult dental care, psychology, and podiatry services.

[6] Edwin Park and Judith Solomon, *Proposal To Establish Federal Medicaid "Blended Rate" Would Shift Significant Costs to States* (Center on Budget and Policy Priorities: June 24, 2011).

[7] Under the ACA, individuals with incomes at or below 138 percent of the federal poverty line, or $15,028 for a single person in 2011, would automatically be eligible for Medi-Cal. Edwin Park and Judith Solomon, *Proposal To Establish Federal Medicaid "Blended Rate" Would Shift Significant Costs to States* (Center on Budget and Policy Priorities: June 24, 2011).

[8] In addition, the ACA increases the federal contribution for Healthy Families from 65 percent of costs to 88 percent from 2015 through 2019.

[9] Federal funds exclude temporarily enhanced federal matching funds provided to states by the American Recovery and Reinvestment Act of 2009. Personal communication with the California Department of Health Care Services (July 1, 2011).

[10] Congressional Budget Office, *Budget Options Volume I: Health Care* (December 2008), p. 137.

[11] The share of individuals reflects non-elderly adults with disabilities and is based on the January 2007 beneficiary count. Expenditures reflect the 12-month period ending September 30, 2007. *California Health Care Almanac: Medi-Cal Facts and Figures* (California HealthCare Foundation: September 2009), p. 36.

[12] The share of individuals is based on the January 2007 beneficiary count. Expenditures reflect the 12-month period ending September 30, 2007. *California Health Care Almanac: Medi-Cal Facts and Figures* (California HealthCare Foundation: September 2009), p. 36.

[13] CBP analysis of 2009 Office of Statewide Health Planning and Development data.