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State Medicaid Reform First—Before Payment Increases

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Congress needs to get serious about Medicaid. To borrow a medical analogy: If a state is the patient, and Congress is its doctor, giving states a temporary increase in the Federal Medical Assistance Percentage (FMAP) to treat the problems associated with Medicaid is malpractice. Medicaid needs surgery, and increasing the FMAP is like giving it two aspirins instead. The temporary relief is not a cure and will actually make things worse for the program and states when it wears off.

The states and the federal government share the cost of the $350 billion Medicaid program. The FMAP formula gives states no less than 50 cents of each dollar spent, and in Fiscal Year 2009, as much as 76 cents. Each state's FMAP is based on its per capita income relative to the nation. In other words, the poorer a state is, the higher the federal share of Medicaid expenses. The FMAP is recalculated every year and typically results in a slight increase or decrease in the federal share. If the per capita income in the state relative to the rest of the nation rises, the FMAP declines (but to no less than 50 percent).

Rising Costs. Congress has quietly added a provision to the economic stimulus package that would have the federal government pay a greater share of Medicaid for every state for a temporary period. Even states that have significant budget surpluses will benefit in order to give something to everyone. But the temporary relief may actually make it harder on states in the long term.

Let us assume that the total cost of Medicaid in a state is $6 billion and the federal share is 60 percent, leaving 40 percent of the cost to the state ($3.6 billion paid by the federal government, $2.4 billion by the state). Under the new provision, Congress provides a temporary increase in the federal share of four percentage points. In our example, that translates to an increase in the federal share to $3.84 billion and a decline in the state share to $2.16 billion. Let us assume in our example that the state does nothing to reform its Medicaid program in the following year and the total cost has increased by 8 percent and is now $6.48 billion. However, the state share increased, because the FMAP is calculated over a three-year period, during which the state became wealthier compared to the rest of the nation. Thus, the state share is no longer 36 percent nor even the original 40 percent but now 41 percent, or $2.657 billion—an increase of nearly $500 million above $2.16 billion in FY 2009 state spending. The state will have to increase spending by 23 percent from FY 2009 (instead of the 8 percent in program costs) to keep total spending at the same level.

Congress has provided a temporary boost before, as recently as 2003, and few members will want to say no in an election year. But states are in a different situation now. They are better equipped to handle their Medicaid problems, because the Deficit

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Reduction Act of 2005 (DRA) gave states broad new authority to change the old dynamics.

New Flexibility. Prior to the DRA, states had only three options to slow Medicaid spending: (1) cut provider rates, (2) reduce benefits, or (3) decrease eligibility. The DRA provided states with new authority to reorganize their Medicaid programs with flexibility in benefits, appropriate cost-sharing, and a shift in long-term care decision-making from institutions to people.

Before writing another check, Congress should consider how states have used (or ignored) the tools they've been given. Rather than sending money, they should send more reform. Currently, the highest cost populations cannot be put into managed care without a federal waiver. States should have the authority to use managed care for all populations. States that have done so have improved the quality of care and saved money for themselves and the federal government. It should also include safeguards to ensure that states cannot "game" the system to bring in even more federal dollars.

There is precedence for this kind of action. When the Bush Administration worked with California and New York to stabilize financing of hospitals, the states agreed to measurable benchmarks tying money to performance. Telling Massachusetts that "business as usual" was no longer acceptable, the Administration helped to trigger a reform plan that attracted national attention. On a bipartisan basis, Massachusetts officials accepted the challenge of reform rather than just demanding more money to keep doing the same thing.

If Congress is determined to increase funding across the board, it should also re-examine the special considerations given to individual states over the years. Federal law provides unique financing arrangements, including special direct payments for certain states. Collectively, these special arrangements and disputes are worth billions of dollars—funds that could be used to pay for the cost of the temporary payment.

Another way to pay for relief should be to re-examine whether the federal share is appropriate. Why, for example, does Washington provide a match rate as high as 90 percent for certain medical services compared to the national average of 57 percent? And when a state lags behind in shifting funds from higher cost institution-based care to individual- and community-based care, it is, in essence, wasting federal dollars. Should Congress treat such a state the same as one that is saving tax dollars through innovation?

The Case for Need. Congress should also consider some standard of "need." How does a congressman from a "poor" state explain to his or her constituents that more money should be sent to a "wealthier" state that continues to expand public assistance? If that state has the money to expand, why does it need more money for its existing Medicaid program?

And why should a state bother to reform its Medicaid programs if it knows the federal government will hide its problem by simply sending more money?

Medicaid is designed as a partnership. Relief without reform would make the federal government the weaker partner and invite further demands on the Treasury. It also would spark tensions and jealousies between the states. This is another congressional misdiagnosis taxpayers cannot afford.

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