



**Roadmap for a Fair and Equitable Relationship:
California's Request for Federal Flexibility and Monies Owed**

FEDERAL GOVERNMENT REQUESTS

FEDERAL REQUEST	REQUESTEE	RESOURCES FOR CALIFORNIA	
		2010-11	ONGOING
<i>Federal Flexibilities Requested</i>			
Authority to Tailor Medi-Cal Benefits to Beneficiaries with the Highest Need and Control Provider Rates	Congress	Enables state to achieve \$750 million in savings	\$750 million in savings annually
Utilization Controls and Benefit Limits in Medi-Cal	Obama Administration		
Co-Payments and Premiums in Medi-Cal	Obama Administration		
<i>Federal Funds Requested</i>			
Increase the base federal matching rate for Medi-Cal from 50 to 57 %	Congress	\$1.8 billion	\$1.8 billion annually
Medicare Disability Determination Reimbursement	Congress	\$700 million (one-time)	–
Recalculate the “Clawback”	Obama Administration	\$75 million	\$75 million annually
Enhanced FMAP for the “Clawback”	Obama Administration	\$250 million (one-time)	–
Extension of ARRA HHS provisions (including FMAP rate)	Congress	\$2.1 billion	at least \$4 billion annually for extension period
Relief from ARRA Restrictions	Congress	(savings would depend on eligibility changes enacted)	
Expanded Federal Eligibility for Foster Care	Congress	\$86.9 million	\$86.9 million annually
Reimbursement for Incarcerated Aliens	Congress	\$879.7 million	\$879.7 million annually
Reimbursement for Special Education	Congress	\$1 billion	\$1 billion annually
<i>TOTAL Federal Funds Requested for 2010-11</i>		\$6.9 billion	
<i>Additional Health Reform Components</i>			
Enhanced Matching Rate for Expansion Population	Congress	–	\$1 billion (begin. 2018-19)
Higher Matching Rates for Physician Services	Congress	–	\$2 billion (begin. 2018-19)
Enhanced Matching Rates for Administrative Activities	Congress	–	\$400 million (begin. 2018-19)



Roadmap for a Fair and Equitable Relationship: California's Request for Federal Flexibility and Monies Owed

As a result of the national and international economic downturn, spurred in part by lax federal oversight of the financial sector, most states faced budget gaps of unprecedented proportion. California made difficult, but necessary, decisions to close a \$60 billion budget gap and successfully managed its cash reserves to avert a crisis.

California's efforts to cut costs and reduce its budget have been challenged every step of the way by federal court decisions that have halted cuts and mandated increased spending, federal funding formulas that disadvantage our state, insufficiently funded mandates and unaffordable maintenance of effort requirements.

While California is slowly emerging from the recession, economic growth is modest and high unemployment persists. Major revenue declines will continue in future years; without corrective action, California is projected to face a budget gap of \$19.9 billion in 2010-11.

The American Reinvestment and Recovery Act of 2009 (ARRA) funds have assisted states during this economic recession. However, states continue to face fiscal challenges well beyond ARRA's current deadline of December 31, 2010, and an extension is needed.

California needs the flexibility to manage costs and target its programs and resources to those most in need. Federal mandates, including spending requirements, constraints on program reductions and federal court decisions delaying budget reductions have caused the loss of more than \$1.4 billion in budget solutions. California must have more tools to manage its program costs within available state resources. If these are not provided by the federal government, then California will be forced to make additional spending reductions that are within the state's authority, but will devastate many critical state programs including education, health and human services and public safety.

Governor Arnold Schwarzenegger's proposed budget for 2010-11 includes structural changes in the state and federal relationship to address federal constraints on California's ability to manage program costs effectively within available resources and to reimburse the state for monies owed by the federal government.

The Governor's proposed budget for 2010-11 includes eight areas where federal action is needed to establish a fair and equitable financial relationship with the state. The Governor is committed to working with the State Legislature and Congressional delegation to advance these priorities in the context of pending federal health care reform legislation, federal appropriations measures, and other congressional vehicles.

Essential Issues for California's Budget in 2010-11 *(Can be Addressed in Health Care Reform Legislation or Other Vehicles)*

Provide federal program flexibility

California operates one of the least costly Medicaid programs in the nation. California's Medicaid program, known as Medi-Cal, has multiple mechanisms to control utilization of services, such as requiring authorization for the number of days a beneficiary can stay in the hospital and for filling more than six prescriptions per month. Given California's current economic condition and its effect on the state budget, the State requires maximum flexibility to set provider rates, establish limits on services and utilization controls; increase cost-sharing through co-payment requirements and/or premiums; and other programmatic changes, similar to what other states have done to reduce costs. These changes would save an estimated \$750 million in budget year 2010-11. In addition, states need relief from the American Reinvestment and Recovery Act (ARRA) requirements that prohibit states modifying eligibility policies, procedures or methodologies.

Secondly, California continues to be precluded from implementing budget reductions approved by the Legislature and Governor. Federal court decisions have resulted in \$1.4 billion in additional costs or lost budget solutions. Authority for the enforcement of Medicaid requirements should rest with federal agencies. Federal law must be modified to limit standing in Medicaid litigation.

Correct the formula that determines the federal funding ratio for California's Medi-Cal program

The current formula that determines how much the federal government contributes to California's Medi-Cal program, the Federal Medical Assistance Percentage (FMAP), is fatally flawed because it relies on per capita income (PCI). As the U.S. Government Accountability Office (GAO) noted in a 2003 report requested by U.S. Senator Dianne Feinstein, "GAO and others have testified before Congress that the current formula does not address wide differences among states in their ability to fund their Medicaid programs and that the formula's reliance on PCI is the primary cause." As a result, a few extremely high wage-earners distort our per capita income, masking a significant number of Californians living in poverty. As a result, California receives the lowest possible federal share for Medi-Cal (50 percent). Other large states have much higher federal reimbursement rates: Florida receives 54.98 percent, Michigan 63.19 percent, Ohio 63.42 percent, Pennsylvania 54.81 percent, and Texas 58.73 percent. *If California received a more equitable rate that matched the average of the ten largest states and reflected the national average of 57 percent, it would result in an additional \$1.8 billion annually.*

Provide California with federal monies owed

Federal funds must be part of the budget solution because the federal government is part of California's budget problem. A fair and equitable financial relationship must include the federal government reimbursing California for monies owed, including:

Medicare Disability Determination Reimbursement to States: Due to an error made and acknowledged by the Social Security Administration, the Medi-Cal program paid for individuals who should have been covered by Medicare for over 30 years. *This was a nationwide error and California's repayment equals approximately \$700 million.*

Medicare Part D: Since the inception of the Medicare Part D prescription drug program, California has been penalized by a flawed methodology that does not reflect its true costs and, as a result, California has paid more to the federal government than before the program's inception. *A correction in this flawed formula would result in an additional savings of \$75 million annually.*

Enhanced FMAP for the Medicare "Clawback": The federal government has determined that the enhanced Federal Medical Assistance Percentage (FMAP) rate provided by the American Reinvestment and Recovery Act (ARRA) does not apply to Medicare Part D state contributions. Thus, states must continue to calculate the amount of those payments using the pre-ARRA FMAP rates even though each state would have been able to claim the enhanced ARRA FMAP rate if the pharmacy coverage remained under its Medicaid program. This imposes unfair costs on states. For the recession adjustment period, the FMAP used in the calculation should be the enhanced FMAP provided for by the ARRA. *Assuming the continuation of ARRA, the General Fund savings could approximate \$250 General Fund in State FY 2009-10 and FY 2010-11.*

Control the borders and take responsibility for federal prisoners

California has historically been disproportionately affected by illegal immigration resulting from inadequate federal border control. Some of these undocumented immigrants are convicted of crimes and are currently incarcerated within California's state prison system. The federal government must provide better control of the nation's borders, and takeover custody of these individuals and house them in federal prison.

The failure of the federal government to control national borders has resulted in increased costs for California and other. One of the largest cost drivers in our correctional system results from the incarceration of undocumented persons in state prisons. For fiscal year 2009-10, the State of California is expected to spend approximately \$970.3 million from the General Fund on the incarceration of undocumented felons.

While the federal government should be fully funding these costs or housing these inmates, California only receives reimbursement for less than 10 percent of its total costs. For fiscal year 2010-11 the state will receive

approximately \$90.6 million. The federal government should accept responsibility for the incarceration of undocumented criminals or pay states the full cost for this service.

Total estimated savings to California: \$879.7 million annually.

Allow California to reduce its prison health care costs

Since the Federal Court appointed a Receiver in 2006 to take over the correctional medical program the cost of the medical program has more than doubled with little accountability and consideration of the State's fiscal condition. The per inmate costs of medical care in California is double and triple the cost of other states and the federal prison system. California's ratios of clinical staff to inmates are significantly greater than that of other correctional health care programs. Use of contract services and staff overtime has increased dramatically since the appointment of the Receiver. California needs the ability to reduce its per inmate prison health care costs to the level of New York for savings of \$811 million. Going forward, management of the state's prison medical program should return to the state and the Receivership should be terminated.

Fully reimburse for mandated special education costs

With the exception of the one-time ARRA augmentation last year, the federal government has never covered more than about 20 percent of federally mandated Special Education Services costs even though federal law requires that they cover 40 percent of the costs. This funding shortfall, coupled with the requirement of a maintenance of effort, has required California to spend an increasingly higher amount of funding for Special Education, thus diverting funding away from other students. This contribution toward Special Education not only has impacted the state but local school districts as well. However, with the last federal special education reauthorization measure, local school districts were authorized to reduce their contributions, while states have not been afforded the same ability. To fully fund its share of the cost, the federal government would need to augment California's grant by over \$1 billion each year.

Total estimated savings to California: more than \$1 billion annually

Expand eligibility for federal foster care funding

Currently, in order to be eligible for federal funding in foster care, the child and his/her family must have qualified for Aid for Families with Dependent Children (AFDC) as the program existed in 1996 the month the child was removed from the home. The 1996 AFDC income standard has never been adjusted for inflation. California's family income has increased significantly since 1996 and this outdated standard arbitrarily excludes many children from receiving federal funding.

A federal change would bring California's foster care program \$86.9 million in 2010-11.

The American Reinvestment and Recovery Act (ARRA)

Extending ARRA will allow for \$2.1 billion in general fund savings in health and human service programs, including:

- Extension of the Enhanced ARRA Federal Medical Assistance Percentage (FMAP) rate (\$1.5 billion)
- Individuals with Disabilities Education Act (IDEA) extension of IDEA Part C (\$32.9 million)
- Child Support Services Initiative extension (\$20.8 million)
- CalWORKs extension (\$538 million)
- Foster Care and Adoption Assistance extension (\$26.8)

Additional Health Care Reform Components

For health care reform to succeed, Congress must first and foremost give states the flexibility and owed monies – as outlined above - to meet current obligations within the revenues available to the state. In addition, pending federal health care proposals must incorporate additional reform components to ensure that states have the fiscal and programmatic capacity to implement the contemplated Medicaid expansion effectively and equitably.

Define “expansion population” as individuals over 54 percent FPL

All states should be treated equally by fully funding all Medicaid adult populations above a reasonable eligibility level, such as 54 percent of the federal poverty level. This level represents the average of the 7 most populous states with income eligibility below California’s 106 percent FPL level. This approach will ensure that states that have increased Medicaid coverage in past years are rewarded and not penalized for their previous expansion efforts. *Total savings to California: Between \$800 million and \$1 billion in 2018-19.*

Provide a higher federal matching rate for physician services

With health care reform’s expanded Medicaid program, funding in the form of an enhanced federal matching rate for all physician services is needed to provide sufficient access to care and avoid an unfunded mandate. *If Congress were to provide 100 percent federal financial support for reimbursement for all physician services at 80 percent of Medicare, the total savings to California would be \$2 billion in 2018-19.*

Provide higher federal matching rate for administrative changes

Federal health reform will require significant administrative changes to ensure data and claiming systems are in place to effectively implement the various program reforms, especially between Medi-Cal and the new Health Insurance Exchange. Outreach and enrollment efforts will also need to be funded. *If Congress were to provide 90 percent federal financial support for such administrative activities, the total savings to California would be \$400 million in 2011-12.*



Roadmap for a Fair and Equitable Relationship: California's Request for Federal Flexibility and Monies Owed

California's Medicaid Program: Utilization Controls and Benefit Limits

Background: California's Medi-Cal program has multiple mechanisms to control utilization of services, such as requiring authorization for the number of days a Medi-Cal beneficiary can stay in the hospital and for filling more than six prescriptions per month. Given California's current economic condition and its effect on the state budget, the State requires maximum flexibility to impose new or enhanced utilization controls to protect the fiscal integrity of the program, similar to what other states have done to reduce costs.

California will seek federal approval to amend its state plan and establish utilization controls and benefit limits on services for adults where effective in reducing costs in such fast growing service areas as pharmacy benefits and outpatient physician visits.

California Needs Flexibility: There are finite methods to control costs in Medi-Cal, which are reduction of provider rates, reduction in eligibility, and reduction in benefits. California can attain reductions in benefits by either removing them from the State Plan entirely or limiting beneficiaries' utilization of the services.

Data from the Kaiser Family Foundation shows that many states have implemented utilization controls in areas such as hospital inpatient days, services provided by federally Qualified Health Care centers (FQHCs), hospital outpatient and physician visits, and number of prescriptions. California is aware of at least one case where a state, South Carolina (*Charleston Memorial Hosp. v. Conrad* [4th Cir. 1982]), prevailed in litigation when imposing a limit of 12 inpatient days per year after demonstrating that 12 days would meet the need of 88 percent of its Medicaid population.

The Bottom Line: The Obama Administration must approve California's state plan amendment (SPA) to establish stronger utilization controls for certain adult services covered by the Medicaid program.



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California's Medicaid Program:

Provide Authority to Tailor Benefits to Beneficiaries with the Highest Need and Control Provider Rates

Background: As California seeks ways to reduce Medicaid benefit costs, it faces an untenable choice: either eliminate an entire optional benefit or continue to provide a benefit that, as currently structured and governed by federal rules, is unaffordable to the state. Federal requirements such as comparability are at odds with California's need to modify optional Medicaid benefits in order to target resources to those most in need.

As examples, California has attempted to modify two optional Medicaid benefits that represent significant and growing General Fund costs the state can no longer afford: the Adult Day Health Care (ADHC) and In Home Supportive Services (IHSS) programs. In both instances federal courts prevented the state from implementing the reductions on the basis that some beneficiaries would suffer a reduction or elimination of services. The Court took these actions even though California is one of a handful of states that provides the ADHC program and despite the fact that it offers the most expansive IHSS program in the nation.

In contrast, the state has been able to eliminate optional benefits, such as adult dental, without the court finding the state out of compliance. The Courts' actions signal that states which never provide these rich benefits, or that eliminate the entire benefit, are doing no harm to their Medicaid populations, but a state will be penalized if it elects to reduce its rich array of benefits to ensure that limited resources target beneficiaries most in need.

California has also been barred from the courts from reducing program costs by making reductions in provider rates. The only cost saving measures left to the state are those that eliminate benefits or eliminate eligibility categories.

In the Balanced Budget Act of 1997, Congress repealed federal law (the Boren Amendment) and reversed other court determinations which had resulted in the courts, rather than the Centers for Medicare and Medicaid Services (CMS), deciding what rates states have to pay providers. The courts have interpreted other federal law to restrict states' ability to control provider rates and benefits, recreating the problem that Congress endeavored to address in 1997.

California Needs Flexibility: California must have the ability to tailor its Medicaid benefit package and structure rates to ensure that limited resources preserve the health and quality of life for those most in need, enabling the most vulnerable beneficiaries to remain safely in the community. Greater flexibility to tailor the benefit to the neediest individuals makes it less likely that California would be forced to eliminate an entire benefit. In addition, California needs the ability to reduce costs through reductions in provider rates. In the absence of authority to tailor optional benefits in the context of the state's continued fiscal crisis, the federal government and courts are leaving the state with no choice but to eliminate these benefits.

The Bottom Line: Congress must modify federal law to provide federal agencies with sole authority for enforcement of Medicaid requirements and take action to undo court decisions.



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California's Medicaid Program: Co-Payments and Premiums

Background: The Deficit Reduction Act of 2005 (DRA), Public Law 109-171, provides states authority to require cost-sharing, such as co-payments and premiums, by certain Medicaid beneficiaries for select program services using State Plan authority. The provisions allow states to align their Medicaid programs more closely to those of private insurance plans by requiring individuals to pay premiums, deductibles, coinsurance or co-payments on services, including those prone to overutilization or inappropriate utilization by members. This cost-sharing can be at higher levels than previously allowed—up to 5 percent of household income. However, the higher cost-sharing provisions are only available to populations with incomes above 100 percent of the federal poverty level (FPL) and are not allowable for services provided to children.

California Needs Flexibility: Co-payments are an important tool in ensuring that beneficiaries utilize the most appropriate and cost effective services. Without co-payments, services such as physician services, pharmacy, emergency rooms may be prone to over- utilization. Premiums ensure that beneficiaries share in the overall cost of health care coverage. In addition, premiums for higher income Medi-Cal beneficiaries will align the cost-sharing requirements similar to that of California's State Children's Health Insurance program, known as Healthy Families, and other publicly sponsored health care programs. Federal waiver authority is needed on the amounts of co-payments and premiums that can be imposed. This is desired to ensure that the established co-payment and premium amounts are set at an appropriate level to influence a change in behavior towards more appropriate use of physician, pharmacy, and emergency room services, but at a level that would not unduly deter individuals from seeking care when medically necessary. In addition, federal waiver authority is needed regarding the amount of monthly premiums a beneficiary will be required to pay for health coverage. This requirement will ensure beneficiaries appropriately value the health care services and Medi-Cal, like other publicly funded programs, becomes a shared contribution between participants and the state.

The Bottom Line: The Obama Administration must provide an expedited review and approval of the state's waiver authority to implement reasonable co-payments and premiums structured in a manner to better manage program costs and service utilization, consistent with the principles of personal responsibility, shared contribution and ability to pay.



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California's Medicaid Program: Permanently Increase the Federal Share of Financing from 50 percent to 57 percent

Background: The current federal medical assistance percentage (FMAP) formula disadvantages California and underfunds its Medicaid program (Medi-Cal). On average, the federal government finances approximately 57 percent of total Medicaid costs nationally and among the 10 most populous states. The current FMAP formula disadvantages California because of its overreliance on the use of average per capita income (PCI) which overstates California's ability to finance the Medi-Cal program given the high need for services in the state for the millions of low-income residents living in poverty. As the U.S. Government Accountability Office (GAO) noted in a 2003 report requested by U.S. Senator Dianne Feinstein, "GAO and others have testified before Congress that the current formula does not address wide differences among states in their ability to fund their Medicaid programs and that the formula's reliance on PCI is the primary cause." California was specifically highlighted in the report as one of three states in the nation with one of the largest populations in poverty, while ranking 49th in per-capita costs (the second leanest Medicaid program in the United States).

Based on 2008 data, California has the 7th highest per capita income but the 11th highest poverty rate. The FMAP formula's insufficient inclusion of poverty as a factor in determining state capacity to pay has resulted in a significant underinvestment by the federal government in California's Medi-Cal program, the largest Medicaid program in the nation. With few exceptions, California has received the minimum FMAP since the inception of the Medicaid program in 1965.

The federal government has deviated from the FMAP formula in certain situations. Congress has shown a willingness to set a state's FMAP at a predetermined level, to modify the FMAP formula and to hold states harmless from natural decreases in funding based on the annual calculation of FMAP according to the statutory formula. These tools have been used in the interest of economic stimulus for all states, but they have also been targeted based on individual need. For example, Congress raised the Alaska's FMAP from 50 percent to 59.8 percent for the two fiscal years of 1999 and 2000. Congress also raised the FMAP for the District of Columbia permanently to 70 percent, effective in fiscal year 1998.

California Needs Flexibility: Congress should again use its authority to modify the current FMAP formula which is not equitable for California. Revising California's FMAP formula will provide additional federal funding which is needed to stabilize the existing program so that California can continue to provide critical health care services to its most vulnerable populations. Without additional federal flexibility and support, California will be forced to make significant program cuts that will leave vulnerable individuals without coverage at a time when Congress is considering broad Medicaid expansions in the context of federal health care reform. If the flawed FMAP methodology is locked into the federal health reform bill, it will be impossible for California to meet the mandatory Medicaid expansion anticipated in pending reform legislation and health reform will not succeed.

The Bottom Line: Congress must permanently increase the federal share of financing of California's Medicaid program from the current 50 percent to 57 percent. Increasing California's base FMAP from 50 percent to 57 percent would result in about \$1.8 billion in additional federal funds annually.



Roadmap for a Fair and Equitable Relationship: California's Request for Federal Flexibility and Monies Owed

California's Medicaid Program: Medicare Disability Determination Reimbursement to States

Background: For the past 35 years, state Medicaid programs have erroneously paid health care costs for disabled individuals that were eligible for the federal Medicare program. These costs were incurred due to an ongoing error by the federal government in its administration of Social Security programs. In 2001, the Social Security Administration (SSA) acknowledged its error and retroactively certified these individuals eligible for Medicare and also billed the states millions of dollars for retroactive Part B Medicare premiums. The SSA error resulted in California incurring costs for health care that were the responsibility of the federal government and paying Part B premiums for coverage that the federal government never provided. The federal government has failed to reimburse the Medi-Cal program for the health care costs it incurred on behalf of these individuals.

A 2006 federal Office of the Inspector General Evaluation Report entitled "The Social Security Administration's Identification of the Special Disability Workload Cases" identified the scope of the problem. The SSA agreed with the reports findings and recommendations.

California Needs Monies Owed: Recently, the National Governors Association, the National Association of State Medicaid Directors, and the Service Employees International Union sent correspondence supporting the "Special Disability Workload Liability Resolution Act of 2009" to the Act's author, Senator John D Rockefeller, and others on behalf of states negatively impacted by this federal administrative error. An analysis provided by the National Governors Association estimates that state Medicaid agencies have paid at least \$6.5 billion for medical services that Medicare should have covered. Congress must reimburse states for the health care costs inappropriately incurred due to Social Security Administration enrollment errors.

The Bottom Line: Congress must appropriate federal reimbursement to California for the \$700 million in state costs it erroneously paid. This federal payment would be one-time and satisfy any future claims for costs incurred by the state resulting from this error.



Roadmap for a Fair and Equitable Relationship: California's Request for Federal Flexibility and Monies Owed

California's Medicaid Program: Recalculate the "Clawback"

Background: In 2006, the federal Medicare program assumed responsibility for the coverage of drugs for people who are dually eligible for Medicare and Medicaid. In exchange for assuming coverage, states were required to pay the federal government 90 percent of the money that it would have spent to provide drugs for people who are dually eligible the first year of the program (2006), with the percentage decreasing by 1.67 percent annually to 75 percent for 2015 and beyond. These payments are known as the states' Part D "phased down contributions."

Federal law requires that the Centers for Medicare and Medicaid Services (CMS) use 2003 expenditure data to set the baseline for these payments. CMS chose to interpret the law very strictly, only considering states' calendar year 2003 expenses on a cash basis.

As a result, even though California was in the process of implementing multiple aggressive prescription drug cost-containment programs, including aggressive supplemental drug rebates and a significant change in the reimbursement paid to pharmacy providers, all of which occurred after 2003, the federal government did not give credit for these savings to the state.

CMS failed to adjust for the most recent and reliable data from states (as allowed under the Medicare Modernization Act) regarding drug rebate collections. By its action, CMS unnecessarily inflated costs to state Medicaid programs and ignored the intent of Congress, which clearly envisioned states paying less for the prescription drug costs of the dual eligible population. Further, CMS has repeatedly noted that the cost of the Medicare Part D program is less than expected. However, CMS continues to increase the Part D cost per dual eligible, resulting in a 52 percent increase since 2003.

California Needs Flexibility: States were assured that no state would be worse off as a result of the required "clawback" payments, an expectation that California U.S. Senators Feinstein and Boxer underscored in a February, 2006, letter to then-HHS Secretary Michael Leavitt in which they demanded relief from the "massive unfunded mandate on states." CMS should use its authority to consider "such other data as the Secretary may require" or there should be Congressional action to give states credit for rebates collected related to 2003 drug costs and recalculate states' baseline amounts for Medicare Part D phased-down state contributions so that they more appropriately reflect the cost of drugs for dual eligibles.

The Bottom Line: The Obama Administration must fix the flawed federal calculation of the state's Medicare Part D payment to the federal government. This change would result in approximately \$75 million General Fund savings for California annually.



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California's Medicaid Program: Enhanced FMAP for the Clawback Payment

Background: The federal Centers for Medicare and Medicaid Services (CMS) has determined that the enhanced Federal Medical Assistance Percentage (FMAP) provided by ARRA does not apply to state Medicare Part D prescription drug payments to the federal government. Thus, states must continue to calculate the amount of those payments using the pre-ARRA FMAP rates even though each state would have been able to claim the enhanced ARRA FMAP rate if the pharmacy coverage remained under its Medicaid program. This imposes unfair costs on states.

California Needs Flexibility: California asserts that, for the recession adjustment period, the FMAP used in the calculation should be the enhanced FMAP provided for by the ARRA; however, CMS has determined the pre-ARRA FMAP rate should be used. This is a very literal interpretation of the state Part D contribution provisions that is not consistent with the purpose of either the stimulus legislation (to increase funds available to states) or the phased-down contribution provision (which is to require a state contribution based on what the state would have expended from its own funds had there been no Part D).

The Bottom Line: The Obama Administration must allow states to apply the enhanced FMAP provided by ARRA to the Medicare Part D phased-down contribution, thereby allowing additional savings. This is consistent with the intent of ARRA, which provides additional relief to states during this severe economic downturn. Assuming the continuation of ARRA, the general fund savings could approximate \$250 million General Fund in State FY 2009-10 and FY 2010-11.



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California's Medicaid Program: Extension of Enhanced ARRA FMAP Rate

Background: Congress enacted ARRA in 2009 as a way to ensure that states are able to provide essential state services during a time of unprecedented fiscal crisis. Congress increased the Federal Medical Assistance Program (FMAP), the federal share of Medicaid financing, for all states and increased it further for states with high unemployment such as California. California's enhanced FMAP is 11.59 percent, the highest increase allowable under the American Recovery and Reinvestment Act of 2009 (ARRA).

The temporary FMAP increase and other support provided by ARRA is intended to support state programs as demand for services rises due to increased unemployment and states' ability to pay for their share of the program falls with declining state revenue.

The House has included a 6 month extension of the ARRA FMAP in its bill. The Senate has not included this extension. The ARRA extension needs to be in the health care reform legislation so that states can plan their budgets knowing the funding will continue. Not extending the ARRA funding would lead to a catastrophic end of federal support when state budgets have not recovered from the economic recession. Extending the ARRA funding for only 6 months is not sufficient as California's revenue will not have recovered by that time.

California Needs Flexibility: The federal health care reform proposals under consideration by Congress would provide affordable coverage options for low-income individuals; however, enhanced FMAP must continue until reforms are in place so that California and all states can meet the needs of the vulnerable populations served today by Medicaid. Recovery in state revenues and employment are expected to lag economic recovery. An extension of enhanced FMAP is crucial to help states maintain their current Medicaid programs during the transition to health care reform as well as maintain support for other vital state programs. The effect of the recession on California will continue long after the scheduled expiration of the enhanced FMAP provided by ARRA. The Governor's recently announced budget proposal for fiscal year 2010-11 seeks to close a \$19.9 billion shortfall; the State's Legislative Analyst Office is currently forecasting annual operating shortfalls of approximately \$20 billion a year through state fiscal year 2014-15. California's unemployment rate in November 2009 was 12.3 percent – among the highest in the nation.

The Bottom Line: Congress must extend the enhanced FMAP rate for all states provided by ARRA beyond the current expiration date of December 31, 2010. This will provide California with continuation of the 11.59 percent increase. The General Fund savings associated with extending ARRA for health and human service programs would total \$2.1 billion in 2010-11. This savings would add to the \$1.8 billion General Fund savings associated with increasing California's base FMAP from 50 to 57 percent.



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California's Medicaid Program: Relief from ARRA Eligibility Maintenance of Effort Requirements

Background: California has historically supported policies designed to increase coverage under its Medicaid program. Earlier this decade during California's "dot com boom", the state expanded coverage to parents with incomes up to 100 percent of the federal poverty level, implemented continuous eligibility for children for twelve months, and covered seniors and persons with disabilities at higher federal poverty levels. These expansions added approximately 1.2 million individuals under Medi-Cal at an estimated annual cost of \$2.3 billion in total funds.

In addition, California has more generous income eligibility rules than the vast majority of states, such as enrolling families with net incomes of 100 percent of the federal poverty level and then allowing these families to use additional deductions from certain types of income which effectively provides them with an income limit of approximately 130 percent of the FPL without loss of benefits.

While enacted during fiscally healthier times, such eligibility expansions are no longer affordable given the state's severely diminished resources.

California was prepared to implement multiple actions necessary to reduce its budget deficit as evidenced by passage of legislation in Fiscal Year (FY) 2007-08 to increase the frequency of eligibility status reviews of Medi-Cal beneficiaries and the introduction of other proposals to reduce eligibility in FY 2008-09. However, upon passage of ARRA, the State took immediate action to suspend the legislation and rescinded the proposals that were under budget consideration to be in compliance with ARRA maintenance of effort (MOE).

The enhanced Federal Medical Assistance Percentage (FMAP) under ARRA has become an all or nothing impediment for states considering such changes. As a result, the ARRA MOE essentially penalizes California for covering a more expansive population.

California Needs Flexibility: California needs flexibility to reduce eligibility income and coverage levels to align with other populous states and to manage our Medi-Cal program within available state resources. This action will ensure that Medi-Cal continues to provide a sufficient array of necessary benefits and services to the populations most in need and commonly covered in other states.

The Bottom Line: Congress must provide relief from the ARRA eligibility maintenance of effort requirements that prohibit states from having more restrictive eligibility policies, procedures or methodologies than were in effect on July 1, 2008, in order to qualify for the enhanced FMAP. State savings would depend on the eligibility changes enacted and the effective federal sharing rate.



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*California's Foster Care Program:
Increased Funding for Children in Foster Care*

Background: Currently, in order to be eligible for federal funding in foster care in California, the child and his/her family must meet a number of requirements imposed by the federal government. The most significant includes that a family qualify for Aid for Families with Dependent Children (AFDC) as the program existed in 1996 the month the child was removed from the home. The 1996 AFDC income standard has never been adjusted for inflation. As a result, each year fewer and fewer children in California are eligible for federal foster care support.

In addition, federal requirements prevent California from claiming federal funding if the child, through no fault of his/her own, lacks citizenship documentation. California has for years recognized that abused children must be protected regardless of citizenship status.

California Needs Flexibility: California needs eligibility for federal funding to be de-linked from the 1996 AFDC standards for family income and resources. California's family income has increased significantly since 1996 and this outdated standard arbitrarily excludes many children from receiving federal funding.

The federal government must recognize that California is committed to protecting all children from abuse and/or neglect and the federal government should recognize through increased funding for all child welfare cases.

The Bottom Line: Congress must amend the Social Security Act to de-link the 1996 AFDC standards for family income and resources. A federal change would bring California's foster care program an additional \$86.9 million in 2010-11 and annually thereafter.



Roadmap for a Fair and Equitable Relationship: California's Request for Federal Flexibility and Monies Owed

California's Special Education Program Fulfilling the Federal Commitment to the States

Background: With the exception of the one-time American Recovery and Reinvestment Act (ARRA) augmentation last year, the federal government has never covered more than 20 percent of mandated special education services even though federal law requires that it cover 40 percent of the costs.

This, coupled with the maintenance-of-effort requirements, forces California to spend escalating amounts for special education and divert funding away from other students. The contribution toward special education not only has impacted the state but local school districts as well. The most recent federal special education reauthorization gave local school districts the ability to reduce their contributions – states should be afforded the same benefit if they remain required to cover the federal portion.

There are an estimated 680,000 students that are served under the Individuals with Disabilities Education Act (IDEA) in California each year. This is approximately 10 percent of total K-12 average daily attendance in California public schools. Additionally, this figure equates to 10 percent of all children with disabilities that are served under the IDEA in the United States each year (6.686 million as of 2007 according to the National Center for Education Statistics). When compared to other states, California serves 37.7 percent more kids than the next highest state—Texas (494,000 students) and 50.4 percent more kids than New York (452,000), the third highest state.

California Needs Monies Owed: California spends over \$6.2 billion in state, federal and local funds for special education requirements each year. Over the past five years California has only received an average of \$1.2 billion -- or 20 percent of total costs from the federal government each year – falling far short of the required 40 percent reimbursement required in federal law. California has had to come up with its own resources to cover the remaining share of costs for federally mandated special education services.

With the exception of 2008 due to the availability of one-time ARRA funds, the federal government has fallen significantly short of providing all states with the appropriation levels required by IDEA. To illustrate, below is a national comparison of what is required and the actual appropriations.

Year	Federal Requirement	Actual Appropriation	Shortfall
2005	\$12,358,376,571	\$10,890,121,721	-\$1,468,254,850
2006	\$14,648,647,143	\$10,874,425,356	-\$3,774,221,787
2007	\$16,938,917,714	\$11,059,383,154	-\$5,879,534,560

The Bottom Line: Congress must fulfill its commitment to fund 40 percent of special education costs which equals an additional \$1 billion in federal special education funding for California.



Roadmap for a Fair and Equitable Relationship: California's Request for Federal Flexibility and Monies Owed

California's Prison System: Reimbursement for Managing the Homeland Security Threat of Undocumented Violent Career Criminals.

Background: California's prisons hold an average of 168,000 offenders, including approximately 22,000 serious felons who are illegally in the US. These felons include, again on average, about 3,500 murderers, 3,600 sex offenders, 2,700 violent criminals and 2,500 armed robbers, according to the California Department of Corrections and Rehabilitation (CDCR). These unrepentant, extremely ruthless offenders run their criminal enterprises – including international drug cartels – from prison cells, holding entire communities hostage to waves of serious criminality.

This is more than a Department of Justice concern; it is also a Department of Homeland Security threat. USDOJ and USDHS should have a strong interest in developing innovative approaches to and management of the security of high-level foreign gang members and predatory felons. These offenders are life-long gang members and thugs, whose ability to reach beyond prison walls must be stopped. The federal government annually appropriates funds for state grants to reimburse for this population.

California Needs Money Owed: It costs California taxpayers nearly \$1 billion dollars yearly to incarcerate these individuals, yet California is expected to receive less than \$100 million in federal reimbursement, even though protection of our borders is a federal, not state, responsibility. California is seeking a collaborative approach with Congress and multiple federal agencies to provide sufficient financial resources to protect the public from 20,000 felons who are in the US due to lack of federal border security. If such financial resources are not forthcoming, the federal government should relieve California of this burden and care for these prisoners themselves.

The Bottom Line: Over the past 15 years, this increasingly serious problem has been inadequately addressed by the federal State Criminal Alien Assistance Program. California's current costs to imprison criminal aliens are nearly \$1 billion, for which the SCAAP will provide less than \$100 million. California should be paid the \$879.7 million it is owed for a lack of federal border protection or allow California to transfer the undocumented prisoners to federal jurisdiction.



**Roadmap for a Fair and Equitable Relationship:
California's Request for Federal Flexibility and Monies Owed**

***HEALTH CARE REFORM: California's Medicaid Program:
Enhanced Matching Rate for Expansion Populations***

Background: California's Medicaid Program, known as Medi-Cal, is the largest Medicaid program in the nation serving approximately 7.4 million individuals. This number is expected to grow by approximately 1.6 million to 1.8 million under health care reform. Of the ten largest Medicaid programs based on enrollment, the income limits of parents covered under Medi-Cal place California as one of the top three states with the highest income eligibility. Of the remaining seven states, the average income limit of parents is approximately 54 percent of the federal poverty level. California's income eligibility limit for parents in Medi-Cal is much higher, at approximately 106 percent of the federal poverty level. At its current enrollment levels, or at levels proposed in the future in response to health care reform, California is unable to financially sustain its Medicaid program with the existing federal matching percentage rate of 50 percent. While there has been some fiscal relief from the federal stimulus funding, it has not been sufficient to relieve the fiscal pressures California faces or prevent programmatic reductions relative to benefits and provider reimbursements.

California Needs Flexibility: The Medicaid expansions under health care reform will lock California into covering individuals at higher income levels and require the state to continue to pay half the cost for populations below 106 percent of poverty. These federal rules are financially unsustainable for California today and going forward. In addition, such rules will result in states that have made little or no effort to expand coverage to low-income families being rewarded with a higher percent of federal funding, while states like California are punished with costs that other states never incurred. Revising health reform's definitions of "expansion" populations would give recognition to historical efforts California has undertaken in developing a comprehensive Medicaid program covering a significant number of low-income individuals and would financially prepare California to take on the new populations proposed under health care reform. In the absence of such a change in the definition of "expansion," California will also face an unfunded mandate when a large number of eligible, but not enrolled, individuals enroll in Medi-Cal due to the individual mandate.

Without this redefinition of the expansion population, Congress would in effect be penalizing California for expanding eligibility beyond the level of the most populous states, while rewarding other states for maintaining very low income eligibility levels in advance of national health care reform. Absent significant federal relief, the state must consider major modifications to the Medi-Cal program, including eliminating optional eligibility categories. This is directly counter to the goals of the Obama Administration and Congress.

The Bottom Line: Congress must define "expansion" populations under pending health care reform as adults who have incomes at or above 54 percent of the federal poverty level for purposes of enhanced federal funding at 100 percent (FMAP).



Roadmap for a Fair and Equitable Relationship: California's Request for Federal Flexibility and Monies Owed

HEALTH CARE REFORM: California's Medicaid Program: Higher Matching Rates for all Physician Services

Background: Increased physician services rates will be essential to attract and retain the expanded supply of providers that will be required to appropriately serve the 1.6 to 1.8 million additional beneficiaries expected to enroll in the California Medicaid program (Medi-Cal) under health reform. While the health care reform proposal passed by the House of Representatives includes an enhanced Federal Medical Assistance Program (FMAP) rate of 80 percent for primary care services, neither the House nor the Senate proposal has any support for increased rates for other physician services.

While primary care is important, it only represents 26 percent of all Medi-Cal fee for service physician payments. It will be critical to address rates for the remaining 74 percent of physician services to ensure patients have an adequate network of specialists available to treat conditions identified by primary care providers as needing treatment by a specialist.

Under federal health care reform, a substantial portion of the currently uninsured population will be obtaining Medicaid coverage and seeking services. Current Medi-Cal rates are substantially below the levels of payment provided by other state Medicaid programs; California is ranked 47th in the nation and pays substantially less than Medicare for similar services. In 2008, the Kaiser Family Foundation reported that Medi-Cal provider rates for all services averaged 56 percent of Medicare rates with primary care rates at 47 percent of Medicare rates.

Currently, there are approximately 130,000 providers enrolled with Medi-Cal in the fee-for-service system. Many of these providers do not participate extensively due in part to the payment levels. While rates are adequate to ensure sufficient access, a small number of providers care for the majority of the Medi-Cal beneficiaries. For example, 10% of the physicians and physician group providers received 81% of all Medi-Cal fee for service payments.

California Needs Flexibility: The increase in provider rates that California and other states will be required to make to maintain access should be considered as a corollary to the 100% Senate funding of "expansion" populations and apply to both primary care and other physician services reimbursements. Otherwise, health care reform is essentially an unfunded mandate on California.

The Bottom Line: Congress must provide in the final health care reform bill 100 percent federal cost sharing (FMAP) for states to increase physician services rates to 80 percent of Medicare. This will enable states like California, with low rates, to increase rates to a level that will ensure sufficient access for the newly insured population. Federal funding participation of 100 percent for physician services rate increases to 80 percent of Medicare would result in an additional \$2 billion in federal funds for California beginning in 2018-19.



**Roadmap for a Fair and Equitable Relationship:
California's Request for Federal Flexibility and Monies Owed**

***HEALTH CARE REFORM: California's Medicaid Program:
Enhanced Matching Rates for Administrative Activities***

Background: Health care reform implementation will require extensive administrative resources in terms of staff resources and system development, implementation and maintenance. One of the critical administrative components needed is for state Medicaid agencies to establish active data exchanges between Medicaid eligibility systems and the data systems used by exchanges to manage health coverage and subsidies for persons receiving coverage through the exchanges. This will require substantial new system enhancement and/or development and maintenance. Proposed health reform will make substantial changes in eligibility categories and requirements that will need to be reflected in the eligibility systems currently operated by states. States will also need to undertake significant outreach and enrollment efforts for the Medicaid expansions and those newly covered by the Exchange.

California Needs Flexibility: Historically, the federal government has provided enhanced funding to promote the development of integrated systems to take advantages of the operational efficiencies that they offer. Also, under the American Recovery and Reinvestment Act, Congress legislated 90 percent federal funding for the administrative activities associated with the state administration of incentive payments for Medicaid providers who adopt and become meaningful users of electronic health records.

The Bottom Line: Congress must provide states with 90 percent enhanced FMAP for the costs associated with the administrative activities of health care reform implementation. These costs are estimated at over \$1 billion in total funds. Of this amount, new system development costs could reach \$700 million in total funds to establish the eligibility management systems needed to manage health care reform. Enhanced funding for administrative costs would provide \$400 million above what the regular FMAP provides for such administrative and systems costs.