CALIFORNIA DEPARTMENT OF HEALTH CARE SERVICES

Managed Care Organization Provider Tax

May 2023

The Department of Health Care Services (DHCS) is proposing to implement a new Managed Care Organization (MCO) tax effective April 1, 2023, through December 31, 2026. The MCO tax provides an additional $19.4 billion in General Fund revenue over this time period. DHCS proposes to use $11.1 billion of this revenue to support additional rate augmentations in the Medi-Cal program. The balance is used to provide ongoing support to the Medi-Cal program.

What is an MCO Provider Tax?

- An MCO provider tax is a federally allowable Medicaid funding mechanism whereby a tax is imposed by states on health care services where the burden of the tax falls mostly on providers, such as a tax on managed care plans per members served. Provider taxes have become an integral source of financing for Medicaid nationwide.
- The MCO tax is used as a mechanism to generate new state funds that can be used to match with federal funds to bring additional federal Medicaid dollars to California.

How Does It Work?

California "taxes" MCOs, otherwise known as managed care plans, and uses the revenue to draw down federal matching funds to support the Medi-Cal program. Specifically, California:

1. Imposes a tax on all managed care plans per members served in a prior year.[1]
    a. The tax varies for Medi-Cal managed care plans compared to non-Medi-Cal managed plans or other managed care plans as seen in proposed budget language.
    b. The fee also has tiers based on the number of members served by the managed care plan. Some tiers have no fee and some tiers cap the number of members the fee applies to in that tier.
2. Runs several "tests" based on federal rules to ensure the tax structure meets all federal requirements.
3. Increases the rates the state pays to Medi-Cal managed care plans to account for the tax. As such, there is no net impact to Medi-Cal managed care plans.
4. Uses the collected funds to secure a federal match to support the Medi-Cal program, which results in a General Fund gain.

May Revision Proposal Details

- Implements a three and three-quarter year MCO Tax beginning on April 1, 2023, through December 31, 2026, resulting in:
    - $3.7 billion in the calendar year 2023 (April-December)
    - Approximately $5 billion per calendar year from 2024 to 2026

[1] By utilizing a prior year, the total amount due for each year is known at passage.

  - **$19.4 billion total over the entire proposed MCO tax period with $11.1 billion available to support additional rate augmentations in the Medi-Cal program. The balance is used to provide ongoing support to the Medi-Cal program.**
  - No net impact to Medi-Cal managed care plans, and minimal impact to a subset of non-Medi-Cal managed care plans.
- A general goal of DHCS' approach is to invest in Medi-Cal system priorities in ways that provide maximal additional federal matching funds to the Medi-Cal system. This requires DHCS to assess the different approaches to sustainable rate augmentations which optimize this approach. In the Governor's proposed May Budget Revision, the following categories of investments are proposed:
  - Effective January 1, 2024, increase base rates to at least 87.5 percent of Medicare for primary care (Nurse Practitioners and Physicians Assistants); maternity care (OB/GYNs and doulas); and non-specialty mental health services. This will be accomplished by eliminating the 10 percent provider payment reductions from AB 97 (Chapter 3, Statutes of 2011) and treating any relevant Proposition 56 supplemental payments as part of the base rate.
    - These immediate investments support DHCS' Comprehensive Quality Strategy and its clinical focus on children's preventive care, maternal care and birth equity, and behavioral health integration, aligning our efforts toward upstream preventive and primary care interventions.
  - Additional rate increases to be effective January 1, 2025, will be evaluated for other provider categories (primary care, maternity care, non-specialty mental health, specialty care, outpatient, and acute care) to support member health, advance quality outcomes, and address health equity.
  - This approach focuses on how to increase the commitment of providers to serve Medi-Cal members, support providers in disproportionately impacted areas, and build robust teams and programs with a strong and well-supported workforce to ensure care is provided in the right settings, at the right time, and at the highest quality.
  - The revenue generated by the MCO tax will be distributed over 8-10 years to provide certainty to providers with rate increases as state is likely to not receive approval for a similar sized MCO tax post 2026.[2] This strategy will allow the focused Medi-Cal augmentations to be sustainable over a long period of time and give certainty to program providers while attending to the state's need of not creating outyear budget cliff.
- In order to maximize the benefit, the MCO tax proposal must be passed by the state Legislature and signed by the Governor in time for DHCS to submit the proposal to CMS, no later than June 30, 2023.

History of the MCO Tax in California

The MCO tax has existed for nearly 20 years and been enacted by both Democratic and Republican governors. The latest MCO Tax expired on December 31, 2022.

[2] CMS has indicated they will be issuing new MCO Tax guidelines that will be more restrictive no later than 2026.

- In 2005, California enacted a quality improvement fee on all premiums paid to MCOs providing coverage to Medi-Cal members.
- AB 1422 (Chapter 157, Statutes of 2009) imposed a gross premium tax on the total operating revenue of Medi-Cal managed care plans until July 1, 2011.
- ABX1 21 (Chapter 11, Statutes of 2011) 2011 – extended the prior MCO tax from July 1, 2011, to July 1, 2012.
- SB 78 (Chapter 33, Statutes of 2013) extended the MCO tax sunset date from June 30, 2011, to June 30, 2013.
- SBX2 2 (Chapter 2, Statutes of 2016) authorized an MCO tax that resulted in approximately $1.5 billion a year from July 1, 2016, through June 30, 2019.
- AB 115 (Chapter 348, Statutes of 2019) and SB 78 (Chapter 38, Statutes of 2019) authorized a successor MCO tax from July 1, 2019, through December 31, 2022, similar to the 2016 MCO Tax.