Department of Health Care Services
Managed Care Organization Tax Update
May 2023

BACKGROUND

The Governor's Budget proposed a multi-year managed care organization (MCO) tax, starting January 1, 2024 through the end of 2026 that was similar in structure to the MCO tax that expired at the end of 2022 and resulted in approximately $2 billion in General Fund revenue annually, and used the MCO tax revenue to achieve a balanced budget. Additionally, the Governor's Budget acknowledged the opportunity to evaluate an increase to the proposed MCO tax at May Revision so as to increase support of the Medi-Cal program.

The Department of Health Care Services (DHCS) has engaged in multiple technical assistance conversations with the federal Centers for Medicare & Medicaid Services (CMS) about the MCO tax and how to design a model that will meet California's goals and also be approvable by CMS.

PROPOSAL

The Administration proposes to update the MCO tax model with the commitment to invest additional funds in the Medicaid program to improve access and equity. The May Revision proposes to begin the MCO tax on April 1, 2023, 9 months earlier than planned at Governor's Budget. This earlier start results in approximately $3.7 billion in additional General Fund revenue that was not accounted for in the Governor's Budget. To do this, DHCS must submit its MCO tax proposal to CMS by June 30, 2023.

Additionally, the Administration proposes to increase MCO revenue (as compared to Governor's Budget) to achieve an approximately $5 billion annual state benefit ($19.4 billion over the proposed MCO tax period). DHCS would note in conversations with CMS, CMS has declared intention to change federal regulations associated with Health Care Related Taxes. Given this intention, this proposed model may not be approvable in the future and DHCS cannot assume we will receive $5 billion in state benefit beyond calendar year 2026. However, DHCS remains committed to maximizing all opportunities in the future.

Therefore, the Administration proposes to: 1) use $2.5 billion of the 2023 net revenue to continue supporting the Medi-Cal program and achieve a balanced budget; and 2) in accordance with our conversations with CMS, the additional $11.1 billion remaining will support Medi-Cal investments that will help secure access, quality, and equity in the Medi-Cal program over an 8-10 period, including the May Revision proposal to increase rates to at least 87.5% for specified providers. Of this amount, $10.3 billion will be put into a special fund reserve for future consideration. 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 challenges.

Effective January 1, 2024, the Administration proposes to increase rates to at least 87.5% of Medicare for Primary Care (inclusive of Nurse Practitioners and Physician Assistants), Maternity Care (inclusive of OB/GYN and doulas) and non-specialty mental health services. The cost of the rate increases, inclusive of the Designated State Health Program (DSHP) rate increase in the Governor's Budget, will be approximately $237 million ($98 million General Fund) in 2023-24, $580 million ($240 million General Fund (in 2024-25, and $582 million ($241 million General Fund) in 2025-26 and ongoing.

These rate increases will be funded by the MCO tax and be an adjustment to base rates, including the elimination of the historical AB 97 reduction and accounting for the Prop 56 supplemental payments. This is important because these rate increases are passed on directly, efficiently, and consistently to the providers. Additionally, the state will direct managed care plans pay providers at least these rates. These investments support the department's 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.

In addition to these changes that will be reflected in the May Revision, and following the submission of the MCO tax to CMS, DHCS, in collaboration with key stakeholders in the Medi-Cal delivery system and with a focus on enhancing equitable access to care, will assess which ongoing, long-term rate augmentations will deliver the greatest benefit to improving Medi-Cal systems across California. The focus will be to look at additional augmentations to primary care, maternal care, behavioral health, as well as specialty care, outpatient and acute care systems with attention on how to increase the commitment of providers to serve Medi-Cal beneficiaries, support providers in disproportionately impacted areas, and build robust teams and programs, with a strong workforce, to ensure care is provided in the right settings, at the right time and at the highest quality.

Following this process, DHCS will return with a proposed set of investments and augmentations that will be put forward to the Legislature in the 2024-25 Governor's Budget, with an intended effective date of January 1, 2025. It is estimated that the model could achieve $3.7 billion total fund ($1.5 billion General Fund/MCO Tax) annually for ongoing rate increases beginning in 2025 for roughly 8 to 10 years, contingent on the finalization and approval of the proposed plan.