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Health Reform Issues: State Financing and Medicaid

Leading health reform proposals in both the House and the Senate include a Medicaid expansion to help eliminate state variation in the current program and to broaden health coverage for more low-income Americans (including childless adults who are now generally barred from Medicaid coverage). Because Medicaid is a program that is jointly administered and financed by states and the federal government, changes to Medicaid will have direct impact on states. While health reform legislation could have many implications for states, the following brief highlights some of the potential benefits and costs to the states associated with Medicaid expansion in the reform proposals.

The recession is placing immediate strains on Medicaid; providing continued federal relief to support increasing Medicaid enrollment during the on-going recession strengthens Medicaid's role for health reform. As states started their fiscal year 2010, the national unemployment rate climbed to 9.8% in September 2009, up from 4.9% in December 2007 at the start of the recession; state tax revenues declined by 16.3% for the second quarter of 2009 (April through June), and states were facing budget gaps of at least \$350 billion for FY 2010 through 2011. At the same time, demand for public programs, including Medicaid continues to accelerate at the time states are least able to pay for these programs. States received significant relief (about \$87 billion from October 2008 through December 2010) from the American Recovery and Reinvestment Act (ARRA) in the form of an increase in the federal share of Medicaid on the condition that states not restrict Medicaid eligibility or make it more difficult to apply for or renew Medicaid coverage. These funds helped states to close budget shortfalls, avoid or soften cuts to providers and benefits and preserve eligibility for Medicaid. However, these funds are set to expire at the end of 2010 (half-way through state fiscal year 2011) creating a financing cliff at a time when most states are not expecting a full economic recovery. Continuation of the Medicaid ARRA funds and the maintenance of eligibility requirements will help put states in a stronger position to implement health reform.

Studies show that there are significant costs if health reform is not enacted. Looking at current trends, one recent study by the Urban Institute shows that within the next 10 years, without health reform the number of uninsured will grow by at least 10 percent in every state, employer sponsored coverage will continue to erode, Medicaid and CHIP spending could grow by 75 percent and uncompensated care would more than double in 45 states.¹ These trends would mean significant increases in demands for state funding for Medicaid, CHIP and uncompensated care costs. Medicaid currently accounts for 17% of state general fund spending, second to spending for elementary and secondary education.

National health reform proposals seek to provide additional federal funds to cover proposed costs of Medicaid expansions that are likely to exceed new costs for most states. Both the Senate and House health reform proposals would include significant federal assistance in financing the costs of the Medicaid expansion. The House proposal would provide full federal financing for Medicaid expansions until 2015 when states would need to contribute 10 percent of the costs. The Senate financing proposal is a bit more complicated and varies across states; however, the FMAPs would be adjusted over time so that by 2019, all states will receive an FMAP increase of 32.3 percentage points for those newly eligible. The Congressional Budget Office (CBO) estimates that the federal government would pay about 90% of the costs for new eligibles. So, under both proposals, even if states are required to contribute 10% of the costs for expansion groups, the federal government will pay 90% which will result in significant amounts of new federal revenue coming into the states. States with higher uninsured rates and lower Medicaid eligibility (typically states in the south and west) are likely to see the largest increases in coverage and new federal revenue. Health reform is also likely to increase participation among those already eligible for Medicaid which will also

¹ Bowen Garrett, John Holahan, Lan Doan and Irene Headen. "The Cost of Failure to Enact Health Reform: Implications for States." Robert Wood Johnson Foundation and Urban Institute, September 2009.

increase costs. This may be especially true for states that have already expanded Medicaid to higher income levels and would be faced with maintenance of eligibility (MOE) requirements. States will be reimbursed at their current match rates (not the enhanced match rates) for most of these increases in enrollment. The fiscal impact for states will vary based on what is assumed about participation rates for both newly eligible and currently eligible groups. Other Medicaid provisions in leading health reform proposals that could result in costs or savings to the states are related to what happens with CHIP enrollees, changes to reimbursement for prescription drugs, new benefit requirements and reductions in disproportionate share hospital payments (DSH).

Expanded Medicaid coverage will increase access to care, reduce unmet health care needs, and improve quality. Both children and adults covered by Medicaid are much more likely to have a usual source of care than people without insurance. Children with Medicaid are also far more likely to have seen a doctor and dentist, and adults with Medicaid are far more likely to get preventive care than the uninsured. Across these measures of primary and preventive care, access in Medicaid and private insurance is roughly equivalent, even though Medicaid enrollees are sicker and more disabled than those with private insurance and despite concerns about low provider participation rates. Enrollment in public coverage is associated with improved quality of care among previously uninsured children as well as improvements in social health outcomes, including school attendance.²

Medicaid expansions will yield economic gains for states and reduce uncompensated care costs. Medicaid spending generates economic activity including jobs, income and state tax revenues at the state level. Medicaid's economic impact is intensified because state spending on Medicaid draws down federal matching dollars. Medicaid funding supports jobs and generates income within the health care sector and throughout other sectors of the economy due to the multiplier effect. The magnitude of the impact is dependent on state Medicaid spending and a state's matching rate (FMAP).³ Some estimates show that every one dollar invested in Medicaid would generate nearly three dollars in new business activity, but can go up to a 6:1 return in Mississippi given the high match rate there.⁴ Under health reform, the federal match for new expansions could be about 90 percent which could significantly increase these estimates for new business activity in most states. Expanded Medicaid coverage is also expected to reduce costs for uncompensated care costs.⁵

Additional and / or alternative assistance could help states better manage the multiple responsibilities associated with implementation of health reform. Under current reform proposals, additional federal financing is largely tied to individuals that would be newly eligible for Medicaid. This structure does not address current Medicaid financing problems and may set up longer-term inequities in financing across states. Alternative options to help support states could be consolidating Medicare-related costs at the federal level (such as costs for Medicare premiums and cost sharing for low-income Medicare beneficiaries or the clawback payment for prescription drug coverage for individuals dually eligible for Medicare and Medicaid) or increasing federal matching rates. In addition, states are expected to have new administrative responsibilities as part of health reform. The current recession has resulted in cutbacks in Medicaid administration in terms of staff and funding. A strong base as well as new investments in Medicaid administrative capacity (staffing and infrastructure) will be necessary to smoothly implement new increases in Medicaid enrollment as well as overall health system changes as part of health reform.

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² Kaiser Commission on Medicaid and the Uninsured, "Medicaid Beneficiaries and Access to Care," October 2009.

³ Kaiser Commission on Medicaid and the Uninsured, "The Role of Medicaid in State Economies: A Look at the Research," January 2009.

⁴ Peter Shin, Leighton Ku, D. Richard Maurey, Brad Finnegan and Sara Rosenbaum, "Estimating the Economic Gains for States as a Result of Medicaid Coverage Expansions for Adults," RCHN Community Health Foundation Research Collaborative. October 2009.

⁵ Bowen Garrett, John Holahan, Allison Cook, Irene Headen and Aaron Lucas, "The Coverage and Cost Impacts of Expanding Medicaid," Kaiser Commission on Medicaid and the Uninsured, May 2009.