Policy Summary: Limiting State Directed Payment Programs (SDP)

Proposals Under Review

There are several proposals under consideration that would limit the size and growth of Medicaid state directed payment programs (SDPs) including the repeal of the Biden administration's Managed Care Final Rule provision to use Average Commercial Rate (ACR) as the benchmark. There may also be other proposals under consideration to apply a cap on the size of SDPs as a percentage of total Medicaid managed care spend.

Estimated Ten-Year Savings (2025-2034) - House Republicans' Estimated Savings: Up to $25B over 10 years[1]*. Relatedly, note that the latest Paragon Health Institute Report estimates potential savings of $200B over ten years if the ACR provision in the Managed Care Final rule is repealed. A recent Arnold Ventures report estimates potential savings from reducing the benchmark for SDPs of up to $120B over ten years*.

Background

In the 2016 Medicaid Managed Care Rule, the Centers for Medicare and Medicaid (CMS) permitted several different types of SDPs as an option to allow states flexibility in financing their programs. SDPs enable states to tailor payment structures to meet the specific needs of their Medicaid populations, allowing for targeted investments in particular services, populations, or healthcare providers. In April 2024, the Managed Care Final Rule promulgated the longstanding practice of using the ACR, an average amount paid by commercial insurers for healthcare services, as the SDP limit.

Since 2016, SDPs have grown significantly - the directed payment arrangements approved as of August 1, 2024 are projected to spend a total of $110.2 billion a year, which is nearly a 60 percent increase over the $69.3 billion in projected spending approved as of February 2023.[2] In response to scrutiny from various federal agencies, including the Medicaid and CHIP Payment Access Commission (MACPAC) regarding their size, CMS has discussed more stringent restrictions, including capping payments at the Medicare rate or implementing state-wide caps. Specifically, a statewide cap on total SDP payments in the range of 10-25% of total Medicaid managed care spend had been raised in the proposed Managed care rule but was not included in the final rule. CMS staff as well as policymakers in Congress are likely to continue scrutinizing SDPs and to consider implementing additional restrictions. Key conservative think-tank, Paragon Health Institute identified SDPs as a key area in need of reform and suggested the repeal of the Managed Care Final Rule as one approach to limit the growth of these programs.

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[1] Politico. "GOP budget menu outlines sweeping spending cuts." January 13, 2025. Available at: https://www.politico.com/live-updates/2025/01/13/congress/gop-sweeping-budget-cuts-00198940.

[2] Directed Payments in Medicaid Managed Care, MACPAC, October 2024.

Historical Traction

Approaches to SDPs have varied across different administrations. The Obama administration supported state flexibility and aligned funding with program goals, allowing states to experiment with SDP models to enhance health outcomes and cost efficiency. The Trump administration modified Medicaid managed care rules and adjusted the oversight of beneficiary protections to provide states more discretion in setting managed care standards. This included the Medicaid Fiscal Accountability Rule (MFAR) in 2019 that proposed new limits on supplemental payments to physicians and other practitioners to 50% of base payments (or 75% of base payments for rural areas and services in designated health professional shortage areas). MFAR was withdrawn in 2020 by CMS due to political pushback from a range of stakeholders.

The Biden administration's 2024 CMS Managed Care Final Rule aimed to enhance access and transparency in Medicaid by reinforcing beneficiary protections and addressing network adequacy standards to improve quality care access and accountability in managed care arrangements. Notably, while not adopted into the final rule, the Biden Administration's proposed managed care rule of 2023 included preamble language around a potential cap on SDPs of 10-25% of total Medicaid managed care spend. The volume of directed payment programs approved has grown exponentially —99 during the Trump administration as of December 2020, compared to 214 between July 2021 and February 2022 under the Biden administration.

Key Considerations

- **Impact on States and Providers**
  Implementing limits on SDPs would have significant financial implications as such programs are active in over 40 states and providers rely on these payments to support their Medicaid programs.

- **Historical Pushback on Potential Caps on SDPs**
  The proposed Managed Care Final Rule from 2023 included potential caps on SDPs based on a percentage of total spend. There was significant pushback in comment letters on the proposed rule related to the damaging impact on access and quality of care were such caps to be implemented.

Scenarios Under Review

As discussions on Medicaid's SDP and Directed Payment Programs continue, key scenarios that have emerged include:

- **Reduce limit from Average Commercial Rate (ACR) to Medicare equivalent**

A new limit may be established alongside a repeal of the Managed Care Final Rule provision related to the ACR as the SDP limit. This may need to follow the rulemaking process, depending on the language in statute. If the statute imposes an absolute SDP limit, rulemaking may not be required. If the statute gives discretion to the HHS secretary to impose a limit on SDPs, for example, then they would need to go through rulemaking unless the statute authorizes the Secretary to establish the limit via a different sub-regulatory process.

- **Cap SDP payments to a percentage of total statewide Medicaid managed care spend**

In the proposed Managed Care rule from 2023, CMS included language in the preamble that considered a proposed cap between 10% to 25% of total managed care payments. This approach may be revisited to limit size and growth of SDPs.