



MEMORANDUM

To: Senate Republicans

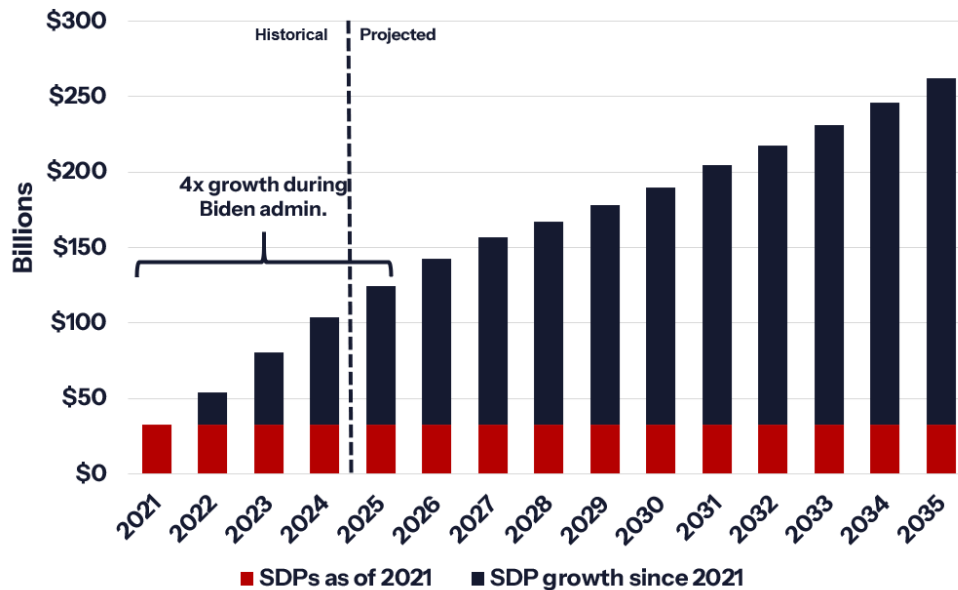
Re: Medicaid Reforms in Senate Finance Committee Released Text

The One Big, Beautiful Bill Act (OBBBA) contains the most comprehensive effort to address waste, fraud, and abuse to preserve and protect Medicaid for the most vulnerable that has ever been considered by Congress. This memorandum describes important issues addressed by the reforms in the text released by the Senate Finance Committee on June 16, 2025.

Background: State-Directed Payments (SDPs) are an extra payment, similar to a tip, on top of the base Medicaid payments that providers receive for providing a service to Medicaid enrollees. The majority of states utilize insurance companies to administer Medicaid and then “direct” these payments through insurers to health care providers, usually hospitals. SDPs are almost always financed by provider taxes and intergovernmental transfers, not state general revenues. Spending on SDPs quadrupled under President Biden, increasing from \$32 billion to \$124 billion per year.

Medicaid State-Directed Payments (SDPs) Spending Exploded After Promotion by Biden Administration

SOURCE: CMS Office of the Actuary



Role in Medicaid Financing Gimmicks: SDPs are often part of schemes used by states to draw down more federal funding than intended under statute. For example:

- Providers willingly volunteer to be subject to special provider-specific taxes with the knowledge they will receive those funds back as even larger Medicaid payments.
- States use SDPs to route money back to providers who contribute the provider tax.
- The arrangement effectively allows states to increase federal Medicaid spending without contributing a state share.
- Without “skin in the game,” states do not have an incentive to spend money as prudently and reimburse providers at much higher rates than they would otherwise.



Biden Administration Actions:

- Because of program integrity concerns, supplemental payments such as SDPs have historically been capped at Medicare rates.
- In 2024, the Biden Administration formalized a policy to allow states to increase SDP rate amounts to average commercial payer rates.
- Studies have found, on average, commercial payers pay more than 2.5 times what Medicare would have paid for the same service. Some states, like California, even have prices that exceed 300% of Medicare.

Effects of Biden Administration Changes:

Welfare Paying More Than Medicare

- A financing mechanism that rewards hospitals more for seeing Medicaid patients than for Medicare patients creates a strong incentive to deprioritize care for seniors.

Poorly Targeted

- According to the Centers for Medicare and Medicaid Services (CMS) Office of the Actuary, just 4.9% of overall Medicaid inpatient hospital spending goes to rural hospitals. This illustrates how financing abuses such as provider taxes and SDPs have not been targeted to the most vulnerable.

Program Integrity Concerns

- Government Accountability Office (GAO): “Rapid Spending Growth in State Directed Payments Needs Enhanced Oversight and Transparency”
- Medicaid and CHIP Payment and Access Commission (MACPAC): “Dramatic growth in opaque Medicaid funding mechanism is exacerbating concerns about the program’s fiscal integrity” (Via HealthcareDive)

Impact of Limiting SDP to Medicare Rates & Addressing Provider Taxes: Aligning SDPs with traditional limits on Medicaid supplemental payments and limiting the provider taxes that fund them will substantially reduce a recent and haphazard explosion of poorly-targeted spending growth in the Medicaid program that has not been associated with increased coverage, improved quality, or expanded access to healthcare providers. The SDP policy would simply revert to one maintained by the Administration of President Obama and taken together, these reforms would free up substantial resources for Congress and the Administration to spend more on intended priorities, such as improving care for vulnerable populations or bolstering financially fragile but critical providers.