DEPARTMENT OF HEALTH & HUMAN SERVICES
Centers for Medicare & Medicaid Services
7500 Security Boulevard, Mail Stop S2-26-12
Baltimore, Maryland 21244-1850

September 29, 2022

Tom Wallace,
Deputy Secretary for Medicaid
Florida Agency for Health Care Administration
2727 Mahan Drive, Mail Stop #8
Tallahassee, FL 32308

Dear Director Wallace:

The Centers for Medicare & Medicaid Services (CMS) is providing this letter as a companion to the approval of Florida's submission of a proposal for delivery system and provider payment initiatives under Medicaid managed care plan contracts (FL_Fee.IPH.OPH4_Renewal _20211001-20220930). CMS understands the important role of sustainable financing and support for safety net providers, including through use of Medicaid state directed payment and permissible health care-related taxes. However, CMS is concerned that the state's use of revenues derived from its Local Provider Participation Program (LPPF) tax program as a source of Florida's non-federal share for payments under this preprint may not comply with certain health care-related tax requirements in section 1903(w)(4) of the Social Security Act (the Act) and implementing regulations in 42 CFR 433.68(f)(3).

As we understand the LPPF arrangement, twenty-one cities or counties impose health care-related taxes on gross or net inpatient and/or outpatient hospital service revenue at a rate of less than six percent. These revenues provide the state with the source of funding for the non-federal share of payments for hospital services that support increased payments to hospitals. Recently, CMS has become aware that other states have similar hospital tax arrangements in connection with which there appear to be pre-arranged agreements to redirect Medicaid payments away from Medicaid providers serving a high percentage of Medicaid beneficiaries to hospitals that do not participate in Medicaid or that serve a low percentage of Medicaid beneficiaries. Florida's LPPF tax structure and media reports indicate that the Florida LPPF arrangement may be similar to other states' arrangements that appear to violate federal requirements. To date, Florida's Agency for Health Care Administration (AHCA) has been unable to provide assurance that there is not an arrangement to redistribute Medicaid state directed payments.

These pre-arranged agreements identified in other states appear to occur with varying levels of state knowledge or direction. Such arrangements appear designed to ensure that participating hospitals are held harmless for all or a portion of their hospital tax costs, which would violate section 1903(w)(4) of the Act and implementing regulations in 42 CFR 433.68(f)(3).

Section 1903(w)(4) of the Act describes what constitutes a hold harmless arrangement. Specifically, Section 1903(w)(4)(C) states that "the State or other unit of government imposing the tax provides (directly or indirectly) for any payment, offset, or waiver that guarantees to hold taxpayers harmless for any portion of the costs of the tax." Implementing regulations at 42 CFR 433.68(f)(3) state that a

hold harmless arrangement exists where a state imposing a healthcare-related tax provides for any direct or indirect payment, offset, or waiver such that the provision of the payment, offset, or waiver directly or indirectly guarantees to hold taxpayers harmless for all or any portion of the tax amount.

In the preamble to the 2008 final rule amending the above-referenced regulation, CMS wrote that "[a] direct guarantee will be found when a State payment is made available to a taxpayer or a party related to the taxpayer in the reasonable expectation that the payment would result in the taxpayer being held harmless for any part of the tax," 73 Federal Register 9694-9695 (Feb. 22, 2008) (confirming proposed rule preamble statement in 72 Federal Register 13730 (Mar. 23, 2007)).

CMS stated that the addition of the word "indirectly" in the regulation indicates that the state itself need not be involved in the actual redistribution of Medicaid funds for the purpose of making taxpayers whole in order for the arrangement to qualify as a hold harmless. CMS further explained in the same preamble that we used the term "reasonable expectation" because "state laws were rarely overt in requiring that state payments be used to hold taxpayers harmless," 73 Federal Register 9694. Therefore, hold harmless arrangements are not always overtly established through state law but can be based instead only on reasonable expectations of certain actions among entities participating in the hold harmless arrangement.

As a result, an arrangement in which hospitals receive Medicaid payments from the state, then redistribute those payments with an aim of holding taxed providers harmless for all or any portion of their cost of the tax would constitute a hold harmless under section 1903(w)(4) of the Act and 42 CFR 433.68(f). Section 1903(w)(1)(A)(iii) of the Act and 42 CFR 433.70(b) require that CMS reduce a state's medical assistance expenditures by the amount of health care-related tax collections that include hold harmless arrangements.

CMS requested information from Florida to ensure that its hospitals do not have pre-arranged agreements to redirect or redistribute Medicaid state directed payments as part of a hold harmless arrangement. In a September 21, 2022 letter, AHCA offered an assurance that it "is unaware of any arrangement between the State or another unit of government and a taxpaying entity involving a payment, offset, or waiver imposing any offset falling within the ambit of § 433.68(f)." This limited assurance differed from previous communication on assurances provided by the state on August 10, 2022. While CMS appreciates that AHCA asserts it is unaware of such an arrangement, this assurance does not address whether hospitals participate in a hold harmless arrangement without state knowledge using Medicaid state directed payments, which include federal Medicaid matching funds.

CMS recognizes that the statute clearly permits certain health care-related taxes and supports states' adoption of these non-federal financing strategies where consistent with federal legal requirements. CMS approves hundreds of state payment proposals annually that are funded by health care-related taxes that appear to meet statutory requirements. All health care-related taxes must be imposed in a manner consistent with applicable federal statutes and regulations and cannot include direct or indirect hold harmless arrangements.

CMS takes its responsibility for financial oversight of the Medicaid program seriously to ensure its long-term health and financial stability. CMS remains committed to ensuring that the non-federal share of Medicaid expenditures complies with all applicable federal requirements, including section 1903(w)(4) of the Act and federal regulations at 42 CFR 433.68(f)(3). At this time, CMS intends to conduct a focused review of the state's LPPF program during Federal Fiscal Year 2023. Should CMS determine that the LPPF tax program involves a hold harmless arrangement, we intend to initiate formal action to reduce the state's medical assistance expenditures before calculating federal financial participation (FFP), as required by section 1903(w)(1)(A)(iii) of the Act. Please note that CMS may seek to recover FFP based on the results of this review, another CMS review, or a review

by another oversight entity (such as the Department of Health and Human Services Office of Inspector General or the Single State Auditor).

CMS recognizes the invaluable role that safety net hospitals play as a critical part of our nation's healthcare infrastructure and as an indispensable asset for ensuring that the most vulnerable in our society receive quality, affordable health care in a timely manner. CMS is available to continue discussions with Florida to ensure its sources of non-federal share meet all applicable federal requirements. CMS is also ready to provide additional technical assistance, including on utilizing health care-related taxes, exploring options for the use of statutorily-permitted tax waivers of broad based and/or uniformity requirements, and ensuring that financing mechanisms are compliant with federal requirements.

Sincerely,

Rory Howe
Director
Financial Management Group
Center for Medicaid and CHIP Services