



DEPARTMENT OF HEALTH & HUMAN SERVICES
Health Care Financing Administration

Center for Medicaid and State Operations
7500 Security Boulevard
Baltimore, MD 21244-1850

June 24, 1998

Dear State Medicaid Director:

A policy concern relating to certain contract requirements on managed care organizations (MCOs) or prepaid health plans (PHPs) has been undergoing Administration review. This is to inform you how we have considered this issue and what decision we have reached.

Some States have required in their contracts with MCOs or PHPs that any savings within their capitated payment, minus an allowed profit, if any, be used to provide health services to persons who are not eligible for Medicaid.

We view this practice as an inappropriate subsidy for services for the uninsured. (See section 1903(m)(2)(A)(iii) of the Social Security Act, which states that capitated programs are intended for Medicaid recipients.)

However, we recognize that when a capitated payment is made to an MCO or a PHP, the entity is required to meet its contractual obligations to serve Medicaid beneficiaries within the money provided, and that except for limits that may be set on allowed profits (in for-profit entities), the MCO or PHP can use its savings as it wishes. In effect, it is no longer "Medicaid money." In fact, should an MCO or PHP voluntarily choose to serve people who are not Medicaid eligible, it is free to do so. However, we believe it is not appropriate for the State Medicaid agency to require in its contract with an MCO or PHP that savings from capitated payments be used to provide health services to individuals not otherwise eligible for Medicaid.

Therefore, for any new or pending section 1915(b) or 1115 waivers (including applications for renewals) or any other Medicaid managed care situation (e.g., State plan option under the Balanced Budget Act), as a matter of policy, we will not approve any State Medicaid agency waiver application that contains a requirement for MCOs or PHPs to use savings under the capitation rate for non-Medicaid eligibles. Furthermore, in our normal review of waivers, Requests for Proposals, and contracts, we will also ascertain whether or not States are in compliance with this policy directive.

If you have any questions about this policy, please contact Wayne Smith at (410) 786-6762.

Sincerely,

/s/

Sally K. Richardson,
Director

cc:

All HCFA Regional Administrators
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