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The Managed Care Tax Replacement:

Implications for Northeast Ohio and the State Budget

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EXECUTIVE SUMMARY

One of the main reasons for the creation of the new Medicaid Health Insurance Corporation (MHIC) tax was the fact that the Centers for Medicare and Medicaid Services (CMS) would not accept the current Managed Care tax as a way for the state of Ohio to draw down federal funds. With this new arrangement, the state will be able to draw down additional dollars, though the state will re-orient the way it pays for services by depositing federal dollars into a dedicated purposes fund rather than the general revenue fund (GRF).

According to Director Keen's testimony, Medicaid's GRF drops by about $2.2 billion in the first year of the budget, increasing by about $430 million the second year (net decrease of about $1.8 billion). The special federal fund group, where the new MHIC dollars will be deposited, grows by about $2.7 billion in year one, and $220 million in year two (net increase of $2.9 billion).

With this in mind, it remains unclear how much of the tax is being allocated to draw down federal funds. If one takes the total amount that could be collected through the new tax (about $740 million) and applies the average federal matching rate of about 2:1, the state could be able to draw down close to $2.2 billion. When the tax and the draw down are combined the net revenue generated is about $2.9 billion, the same amount that is being deposited into the new special fund.

Federal law dictates that Medicaid taxes must be used to pay for Medicaid services. However, as is the case with Medicaid financing, states often leverage the influx of federal dollars to offset their state obligation, freeing up resources for other policy priorities like education or tax cuts. With the new MHIC tax generating $740 million, potentially leveraging a total of $2.2 billion in federal funds, the new distribution of $207 million to the counties represents roughly 7 percent of the total $2.9 billion generated. Moreover, as this tax is temporary, more will have to be understood in terms of how this new tax not only provides temporary relief for counties taking advantage of revenue they were not intended to earn, but how the state will provide long-term structural soundness for administrations in the future, especially as it relates to Medicaid.

BACKGROUND

On February 1st[i], Tim Keen, Director for the Office of Budget and Management, outlined the Governor's final proposed budget[ii] before the new Ohio House Finance Committee. While the presentation highlighted a number of policy proposals, the Managed Care Tax replacement is of particular interest, as it has broad effects not only in terms of state revenue, but also on Medicaid, local government and regional transit.

Ohio has a largely privatized Medicaid program, having contracted out most of the case management of Medicaid recipients to privately-held insurance companies called Managed Care Organizations (MCOs). 2006 is when a tax was first assessed on MCOs, raising revenue not only through state receipts but also through the federal matching process in Medicaid. In Fiscal Year 2009, this amounted to $221.5 million in tax collections with a $489.5 million federal match.

However, as we cited in 2011[iii], Ohio's MCO tax had to be revised to conform to the standards in the federal Deficit Reduction Act (DRA) of 2005, ultimately leading Ohio to develop a work-around policy which transitioned the MCO tax to a sales tax. Importantly, Ohio law allows local governments and regional transit authorities to adopt "piggy back" sales taxes, which enabled local governments to generate millions of dollars on the local level. Ohio's sales tax, though, did not conform to federal standards of being "broad-based and uniform" as it did not also apply to commercial, non-Medicaid insurers. In 2014, the Centers for Medicare and Medicaid Services (CMS), which oversees these regulations, issued guidance to states[iv] explaining that such arrangements were in violation of federal law and such state tax policies would need to be eliminated or changed.

THE PROBLEM

Last summer, in response to this guidance and the impending revenue problem for the state and the local jurisdictions, Director Keen outlined losses[v] that the state and local governments would face to the County Commissioners Association of Ohio (CCAO). Overall, the loss equates to about $850 million per year in sales tax revenue, $300 million of which is used to draw down over $1 billion in federal funds. For local governments and transit authorities, this would mean a loss of around $180 million.

THE PROPOSED SOLUTION

While some argued that the sales tax should be extended to a limited number of insurance companies as defined in Ohio Revised Code section 1751.01(O)[vi], Director Keen's testimony referenced analysis showing it would raise costs to non-Medicaid insurance customers by 7 percent. In order to replace this funding, the Ohio Department of Medicaid (ODM) requested, and has received, a waiver from CMS allowing Ohio to circumvent the broad-based and uniformity requirements to create a new Health Insurance Corporation (HIC) provider tax.

This temporary tax, only in place for this biennium, charges Medicaid HICs a $26-$56 per member per month fee and non-Medicaid HICs a $1-$2 per member per month fee. This

approach was approved by CMS because it determined it was generally redistributive. Here is an outline of the potential impact to HICs:

PROPOSED MHIC TAX

	Non-Uniform Tax
*Aetna**	$ 11,512,816.42
*Buckeye**	$ 95,077,518.47
*Caresource**	$ 360,725,879.03
*Molina**	$ 101,976,507.64
*Paramount Advantage**	$ 71,607,295.96
*United Healthcare**	$ 94,442,488.65
Community Insurance Company	$ 674,836.00
Consumers Life Insurance Company	$ 16,152.00
HealthSpan Integrated Care	$ 130,260.00
HealthSpan, Inc.	$ 152,892.00
Humana Health Plan of Ohio	$ 278,946.00
Medical Health Insuring Corp of Ohio	$ 785,722.00
Premier Health Plan, Inc.	$ 105,624.00
TOTAL	**$ 737,486,938.17**

*Indicates company has a Medicaid plan

Source: The Ohio Department of Medicaid

THE MECHANICS OF THE MHIC TAX

Because this is not a sales tax, local governments aren't able to generate revenue through the MHIC tax. Instead, the state is proposing "transitional support payment", totaling $207 million, which consists of two components[vii]:

4th Quarter 2017 Payment

This is a lump sum payment made to all counties covering the last quarter of 2017 totaling $49 million. The money is a product of the average distribution based on collections in 2015 and 2016 using the tax rate in place at the end of 2016 and then multiplying that amount by 25 percent.

The "Formula" Component

The second component is more complicated, providing $158 million in aid, also via a one-time payment. The 8-step process involves taking the average amount that would have been received under the previous structure, determining the annualized distributions over the next four years and applying an "absorption rate" built on a county's "capacity", as outlined in the table on the next page:

"FORMULA" COMPONENT OF THE MHIC TAX

STEP	NAME	DESCRIPTION	FORMULA	EXAMPLE: CUYAHOGA
1	County MHIC Sales	The average annualized county collections. This will be the ceiling for any distributions.	Average Annualized County MHIC Sales	$25,302,086
2	Sales Tax "Capacity"	Take the average per capita sales tax outside of the MHIC tax between 2015 and 2016 and divide it by statewide average. If below 100%, go to step 3.	Capacity = (County Per Capita) / (Statewide Per Capita)	$15,027 / $14,352 = 104.7%
3	Annual "Incremental Absorption Rate"	Lesser of 4% *OR* (Capacity x 4%).	If Capacity below 100%: (Capacity x 4%)	4% (above 100%)
4	Total Absorption Rate	Total amount to be absorbed by county based on incremental amount in step 3.	Year 1: IAR Year 2: IAR x 2 Year 3: IAR x 3 Year 4: IAR x 4	Year 1: 4% Year 2: 8% Year 3: 12% Year 4: 16%
5	Annualized Total Sales Tax	This is the average of 2015 and 2016 calculated with tax rate of county at end of 2016.	Total Sales Tax = (Average County Collection) x (County Tax Rate)	$258,184,551
6	Annual "Absorption Amounts"	Take each year's absorption rate and multiply it by the total sales tax amount.	Year 1 Annual Absorption Amount = (Year 1 IAR) x (Sales) Year 2 Annual Absorption Amount = (Year 2 IAR) x (Sales) Year 3 Annual Absorption Amount = (Year 3 IAR) x (Sales) Year 4 Annual Absorption Amount = (Year 4 IAR) x (Sales)	Year 1: 4% x $258,184,551 = $10,327,382 Year 2: 8% x $258,184,551 = $20,654,764 Year 3: 12% x $258,184,551 = $30,982,146 Year 4: 16% x $258,184,551 = $41,309,528
7	Final Aid Amount	Take the local MHIC sales tax distribution and subtract each year's absorption amount. If/when the amount is negative, there is no aid given.	Year 1 Final Aid Amount = (MHIC) - (Year 1 Abs) Year 2 Final Aid Amount = (MHIC) - (Year 2 Abs) Year 3 Final Aid Amount = (MHIC) - (Year 3 Abs) Year 4 Final Aid Amount = (MHIC) - (Year 4 Abs)	Year 1: $25,302,086 - $10,327,382 = $14,974,703 Year 2: $25,302,086 - $20,654,764 = $4,647,322 Year 3: $25,302,086 - $30,982,146 = ($5,680,060) Year 4: $25,302,086 - $41,309,528 = ($16,007,442)
8	Total Aid	Sum each year's eligible amount.	Total County Aid = Year 1 Fin + Year 2 Fin + Year 3 Fin + Year 4 Fin	Because Year 3 and Year 4 exceeds $25,302,086, there is no further yield after Year 2. Total = $19,662,025 *(OBM estimate is $18,715,670)*

IMPLICATIONS FOR NORTHEAST OHIO

Here is the current revenue generation for Cuyahoga, the surrounding counties, and the associated transit systems:

	Total Countywide Sales Tax	Previous MHIC Tax	"Q4" Payment	"Formula" Payment	Total Transition Payment	Loss or Gain
Cuyahoga	$ 257,655,465	$ 25,302,086	$ 6,325,522	$ 18,715,670	$ 25,041,192	$ (260,894)
Lorain	$ 28,825,845	$ 2,365,747	$ 591,437	$ 1,833,646	$ 2,425,083	$ 59,336
Medina	$ 24,452,389	$ 963,321	$ 240,830	$ -	$ 240,830	$ (722,491)
Summit	$ 44,373,867	$ 3,298,852	$ 824,713	$ 1,484,489	$ 2,309,202	$ (989,650)
Portage	$ 20,645,675	$ 1,636,714	$ 409,179	$ 759,180	$ 1,168,359	$ (468,355)
Geagua	$ 15,051,414	$ 416,266	$ 104,067	$ -	$ 104,067	$ (312,199)
Lake	$ 35,504,949	$ 1,671,199	$ 417,800	$ 223,163	$ 640,963	$ (1,030,236)
Transit Authority						
Greater Cleveland	$ 205,843,422.00	$ 20,241,668.00	$ 5,060,417	$ 15,007,749	$ 20,068,166	$ (173,502)
Laketran	$ 8,832,168.00	$ 417,800.00	$ 104,450	$ 55,970	$ 160,420	$ (257,380)
Portage Area	$ 5,156,388.00	$ 328,210.00	$ 82,053	$ 152,852	$ 234,905	$ (93,305)
Metro	$ 44,190,357.00	$ 3,298,852.00	$ 824,713	$ 1,490,928	$ 2,315,641	$ (983,211)

Source: Ohio Office of Budget and Management

With the formula outlined by the administration, almost all counties and all of the regional transit systems would see some sort of loss relative to the experience they would have had otherwise. It is important to note, that this estimate does not contemplate the successful "carving in" of new, more expensive populations into Medicaid, such as those with behavioral health issues or the long term care system, which, due to the much higher average cost, would generate significantly more revenue than the current tax. Regardless of these estimates and their construction, losses are considerably mitigated by the new proposal.

WHAT IS NEXT?

Short-Term Solution

Director Keen has indicated that this is a temporary fix for counties, stating in his testimony that these revenues have only been collected since 2010. Indeed, our analysis from 2011 indicated that this source of funding was at risk and likely in violation of federal regulation. Given the recent cuts to local government funding, and due to the increases of revenue share this funding stream has represented to counties since expansion, it is likely that local governments will advocate, on some level, to continue this funding beyond this biennium. In all likelihood, this arrangement may still be difficult to maintain given CMS' reluctance to establish non-uniform taxes. With that said, CMS, in its approval letter, did state that any future changes to the taxing structure, including the non-uniformity provisions, will require a new waiver request.

[i] Budget Testimony (2017) (testimony of Director Tim Keen). https://www.ohiochannel.org/video/ohio-house-finance-committee-2-1-2017

[ii] United States. Ohio Office of Budget and Management. Operating Budget FY 18-19. Columbus, OH, 2017. http://obm.ohio.gov/Budget/operating/fy18-19.aspx

[iii] Honeck, John, PhD. MCO Sales Tax. December 11, 2011. A Review of Ohio's Medicaid Managed Care Sales Tax Policy. https://ccs.memberclicks.net/assets/docs/State_Budgeting_Matters/sbmv7n9mcosalestaxhoneck121511.pdf

[iv] United States. Department of Health and Human Services. The Center for Medicare and Medicaid Services. Health Care-Related Taxes. By Cindy Mann. 001st ed. Vol. 14. SHO. Baltimore, MD, 2014. https://www.medicaid.gov/Federal-Policy-Guidance/downloads/SHO-14-001.pdf

[v] Neithammer, Kate. Impact of Federal Regulations on Ohio sales tax revenue. June 30, 2016. CCAO: Statehouse Report, Columbus, Ohio. https://www.ccao.org/userfiles/SHR06302016.pdf

[vi] Health insuring corporation law definitions, § 1751.01. http://codes.ohio.gov/orc/1751.01

[vii] Description of steps used to calculate the amounts for the proposed Medicaid Local Sales Tax Transitional Aid program. January 30, 2017. http://obm.ohio.gov/Budget/operating/doc/fy-18-19/SchoolFunding/MHIC_Transition_Aid_Calculation.pdf

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