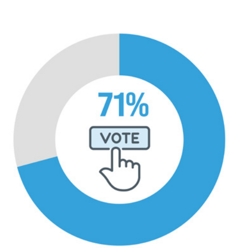
Medicaid Provider Taxes: Restricting Them Threatens Hospitals, the Health Care System and State Economies

States and the federal government jointly cover the costs of health care and services provided to the almost 80 million people covered by Medicaid — a lifeline for children and low-wage working families, veterans, vulnerable seniors and people with disabilities.[1] Provider taxes are core funding mechanisms for the state portion of Medicaid, approved by bipartisan policymakers for decades, that fund almost one-fifth of state Medicaid program costs.[2]

Federal proposals to eliminate or limit state options to generate revenue to pay for their share of Medicaid costs — including banning the use of provider taxes — would gut Medicaid by shifting costs onto states, threatening state and local economies and upending the core financing of the health care system.[3] As a result, states would be forced to offset budget losses by raising taxes on families and businesses, throwing people off coverage, cutting provider funding and eliminating essential health services.



Medicaid must be protected from attempts to make it harder for states to pay for their share of program costs. Proposals that restrict taxes on health care providers or otherwise narrow the funding streams states depend on to finance Medicaid are ultimately just proposals to cut the program. These proposals are a direct attack on the health and financial security of the American people and run counter to public will: **71% of voters want Congress to continue to guarantee coverage for low-income people through Medicaid**.[4]

PROVIDER TAXES ARE ESSENTIAL FOR STATE MEDICAID BUDGETS

Under federal law, states can generate revenue to pay their share of Medicaid expenses through state general funds, income and sales taxes, funding from local government, and taxes and assessment on health care providers and managed care plans.[5] In compliance with federal guidelines, **49 states and the District of Columbia tax one or more type of health care provider or entity** — including hospitals, nursing facilities and managed care plans — to raise a small portion of the funds they need to cover Medicaid expenses.[6] These taxes are known as "provider taxes."

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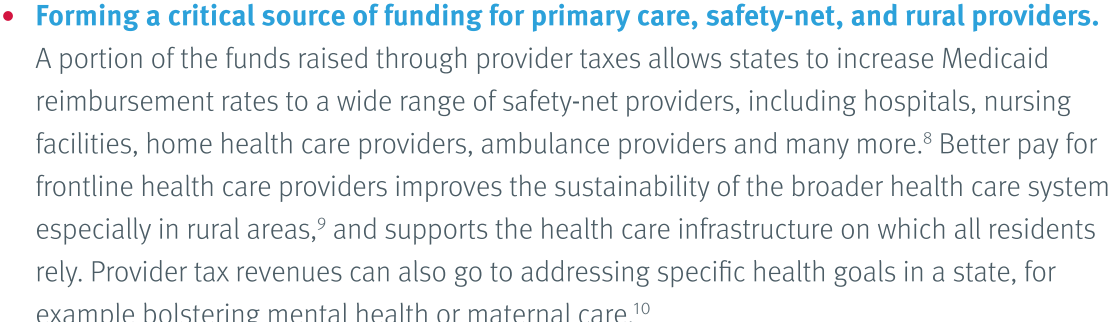
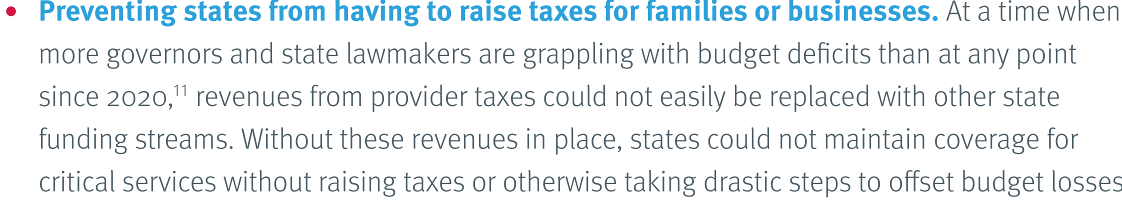
THE BENEFITS OF PROVIDER TAXES

Hospitals and other providers are willing to contribute their fair share to keep Medicaid working in their state because provider taxes serve many important functions, including:

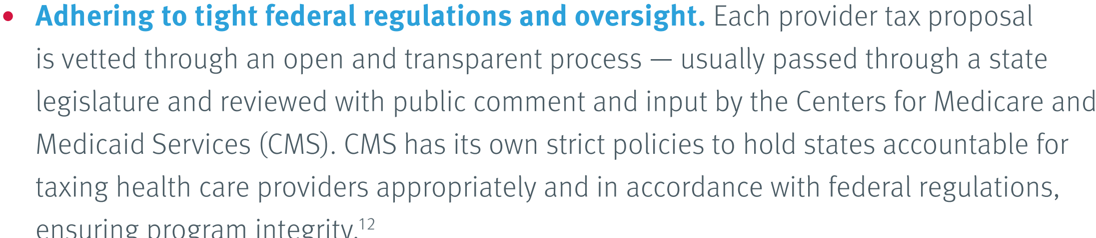
- **Keeping people insured and keeping hospitals open.** Medicaid is a critical funding source for hospitals across the country and especially helps keep rural hospitals open.[7] When people have insurance, they are more able to appropriately access and pay for health care services, alleviating the burden of uncompensated care for hospitals and other providers.



- **Forming a critical source of funding for primary care, safety-net, and rural providers.** A portion of the funds raised through provider taxes allows states to increase Medicaid reimbursement rates to a wide range of safety-net providers, including hospitals, nursing facilities, home health care providers, ambulance providers and many more.[8] Better pay for frontline health care providers improves the sustainability of the broader health care system, especially in rural areas,[9] and supports the health care infrastructure on which all residents rely. Provider tax revenues can also go to addressing specific health goals in a state, for example bolstering mental health or maternal care.[10]



- **Preventing states from having to raise taxes for families or businesses.** At a time when more governors and state lawmakers are grappling with budget deficits than at any point since 2020,[11] revenues from provider taxes could not easily be replaced with other state funding streams. Without these revenues in place, states could not maintain coverage for critical services without raising taxes or otherwise taking drastic steps to offset budget losses.



- **Adhering to tight federal regulations and oversight.** Each provider tax proposal is vetted through an open and transparent process — usually passed through a state legislature and reviewed with public comment and input by the Centers for Medicare and Medicaid Services (CMS). CMS has its own strict policies to hold states accountable for taxing health care providers appropriately and in accordance with federal regulations, ensuring program integrity.[12]

RESTRICTING THE USE OF PROVIDER TAXES WOULD DRASTICALLY CUT STATE MEDICAID BUDGETS

While most state Medicaid expenses are paid from general state budget dollars, approximately 17% of state Medicaid dollars (on average) come from provider taxes.[13] If this portion of Medicaid spending is no longer in place, the Congressional Budget Office (CBO) estimates that states would cut their Medicaid spending by lowering payment rates to providers, cutting optional medical services and reducing program eligibility.[14]

HARMFUL POLICY PROPOSALS TO REDUCE PROVIDER TAXES:	IMPACT OF PROPOSALS ON STATE MEDICAID BUDGETS:
Current proposals would: • Lower the "safe harbor" threshold from the current max of 6% of net patient revenue[15]* (to a range between 2.5% and 5% of net patient revenue[16]); or • Eliminate Medicaid provider taxes altogether.[17]	• **If provider taxes are *limited***, CBO estimates this would reduce federal Medicaid dollars to states between ***$48 billion*** (tax limited to 5% net patient revenue) and ***$241 billion*** (limited to 2.5%) over ten years — blowing holes in existing state budgets, and forcing cuts to coverage, access, benefits and/or services. • **If provider taxes are *eliminated entirely***, CBO estimates that states would have to pay an additional ***$605 billion over ten years to replace lost federal dollars***.[18]

THE BOTTOM LINE: MEDICAID MATTERS TO EVERYONE

Limiting states' ability to raise the funds they need to cover Medicaid expenses is just another way for the federal government to cut its support for state Medicaid programs. Americans from all backgrounds just voted for economic security, imploring their representatives to lower costs on everyday needs, including health care. Proposals that slash the funding streams states depend on to finance Medicaid only shift more costs to states and do nothing to address underlying health care costs for consumers. Any cut to federal Medicaid funding would ignore voters and directly threaten the health and financial well-being for the 80 million Americans who rely on Medicaid for health insurance. Congress has the responsibility to stand with our nation's families by protecting Medicaid and opposing any attempts to weaken this essential program.

For more information or to connect with the Families USA team, please contact healthpolicy@familiesusa.org.

To read the full publication with endnotes, please visit familiesusa.org/Providertaxes

*The Centers for Medicare and Medicaid Services (CMS) sets what is known as a "safe harbor," where if a state taxes health care providers less than a threshold amount—currently set at 6% of net patient revenue—then a state's tax is generally considered to be in compliance with Medicaid regulations. A state can impose a provider tax above the 6% threshold, but then it would have to meet a range of additional requirements. For this reason, states generally do not go above the threshold set by CMS. If the "safe harbor" threshold were lower, states would be likely to reduce their provider taxes accordingly to stay within the threshold. "Limit State Taxes on Health Care Providers," CBO, December 7, 2022, https://www.cbo.gov/budget-options/58623; "Health Care–Related Taxes in Medicaid," Medicaid and CHIP Payment and Access Commission, Issue Brief, May 2021, https://www.macpac.gov/wp-content/uploads/2020/01/Health-Care-Related-Taxes-in-Medicaid.pdf.