Medicaid Supplemental Payments are Essential for Children's Hospitals

In many states, Medicaid base payments – the initial payment to hospitals or other providers for a service provided to a Medicaid beneficiary – do not cover the cost of care and are significantly lower than Medicare and commercial payments. States utilize supplemental payments – any payment over and above base payments – to help mitigate these payment gaps.

Congress is discussing potential reductions to states' use of state directed payments (SDPs). These payments are critical for ensuring access to care for the 37 million children covered by the Medicaid program, especially at children's hospitals. CHA urges Congress to reject policies that would reduce Medicaid payments to children's hospitals.

Children's hospitals are major Medicaid providers, with 55% of their payments coming from Medicaid. **However, Medicaid payments, including supplemental payments, still on average cover less than 80% of children's hospitals' costs of providing care.[1] Supplemental payments allow children's hospitals to continue providing high quality, life-saving services to children across the country. Any cuts to supplemental payments will impact children's hospitals financial sustainability and the care they provide to all children.**

Types of Supplemental Payments

SDPs are payments states may direct to managed care organizations (MCOs) to designated providers to promote access to and quality of care. SDPs are subject to federal approval and have surpassed other forms of supplemental payments, reflecting the shift toward Medicaid managed care.

What are State Directed Payments (SDPs)?

- 40 states use SDPs to raise reimbursement rates for providers treating Medicaid patients.[2]
- SDPs are a critical payment stream in Medicaid that provide children's hospitals with funding to mitigate the financial challenges caused by low Medicaid base payments. For some children's hospitals, SDPs help to fill gaps in payment by an estimated 20%.
- CMS codified in 2024 that states can use the "Average Commercial Rate (ACR)" – the average amount hospitals and other providers would be paid by commercial insurers for the same service – as the payment ceiling for SDPs.[3] Lowering this ceiling to Medicare levels would lead to inadequate payments for pediatric care, since many pediatric services are not reimbursed under Medicare and Medicare rates do not necessarily consider children and their needs.

The Bottom Line

- Children's hospitals make up less than 5% of the nation's hospitals but account for about 45% of all hospital days for Medicaid-enrolled children.[4] Medicaid, on average, provides health insurance coverage for half of children's hospitals patients and for some children's hospitals patient mix, closer to three-quarters.[5]
- Supplemental payments are a critical funding source for children's hospitals who provide care to millions of children across the country. Even with these payments, Medicaid still does not cover the cost of care. Scaling back SDPs would exacerbate the existing shortfall between Medicaid payments and children's hospitals' costs impacting their ability to provide care.

[1] "Children's Hospital Association Annual Benchmark Report," Children's Hospital Association. 2023
[2] "Directed Payments in Medicaid Managed Care," Medicaid and CHIP Access and Payment Commission. October 2024.
[3] Ibid.
[4] Children's Hospital Association Analysis of the Agency for Healthcare Research and Quality's Kids' Inpatient Database (KID), Healthcare Cost and Utilization Project (HCUP). 2019
[5] "Medicaid's Role for Kids and Children's Hospitals," Childre's Hospital Association. April 2023