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

RE: Designated State Health Programs and Designated State Investment Programs

April 10, 2025

Dear State Medicaid Director:

Introduction

The Centers for Medicare & Medicaid Services (CMS) has approved several demonstrations under the authority of section 1115(a) of the Social Security Act (the Act) that provide federal matching funds for state expenditures for designated state health programs (DSHP) and designated state investment programs (DSIP). After reviewing these approvals, CMS has determined these programs were funded entirely without federal Medicaid funds prior to those approvals, and the addition of federal Medicaid funding does not render these programs as integral components of section 1115 demonstration programs. As such, CMS has renewed concerns about the appropriateness of providing federal funding for these programs under section 1115 demonstration authority and does not anticipate approving new state proposals of section 1115 demonstration expenditure authority for federal DSHP or DSIP funding or renewing existing section 1115 demonstration expenditure authority for federal DSHP or DSIP funding, including when current DSHP or DSIP authority concludes before the expiration date of the demonstration. Federal DSHP funding has historically raised oversight concerns about its consistency with the federal-state financial partnership established under the Medicaid statute, and CMS is increasingly concerned about this issue.

Background

DSHPs are programs that were funded entirely without Medicaid funds prior to their approvals and, without CMS's approval under section 1115 demonstration authority, would not have qualified for federal Medicaid funding. Under these approvals, CMS makes these programs eligible for federal Medicaid matching funds through section 1115 expenditure authority, effectively having the federal government share in the costs of funding these state programs. As a result, the state uses the “freed up” state dollars as a non-federal share source for its Medicaid demonstration or for other state purposes. In other words, these demonstrations can effectively function as a technique to reduce states’ overall funding obligation by allowing federal funds to supplant existing state funds for services not otherwise covered by Medicaid. Further, unlike traditional Medicaid matching funds, which are generally tied to claims for specific services provided to Medicaid beneficiaries, federal matching funds provided to support DSHP and DSIP have not necessarily been tied directly to services provided to Medicaid beneficiaries.

Since 2005, CMS has authorized several states to draw federal Medicaid matching funds for DSHP under the authority of section 1115(a)(2) of the Act. In 2017, CMS issued guidance[1] to states indicating it would no longer approve or renew state requests for DSHP authority under section 1115 demonstrations. However, in 2021, CMS approved authority for expenditures, referred to as DSIP, for designated programs that provide or support the provision of health-related services that were otherwise state-funded and are not eligible for Medicaid funding in one state's section 1115 demonstration.[2] Subsequently, beginning in 2022, CMS approved several section 1115 demonstrations[3] that provided federal funding for DSHPs but included limitations on both the size and scope of DSHP. Under the more recent DSHP approvals, states were expected to use "freed up" state funding on demonstration initiatives that CMS determined would be likely to assist in promoting Medicaid objectives, and that would add to the state's Medicaid program, not supplant existing services or programs. Additional parameters and guardrails in these post-2022 approvals included a required state contribution (e.g., general revenue, intergovernmental transfers, etc.) as the non-federal share of the DSHP-supported initiative, a cap on the total amount of federal and state DSHP expenditure authority as a percent of the state's total federal and state Medicaid spending, and a time-limited duration of federal funding for DSHP. Consistent with historical CMS approvals for DSHP, allowable DSHP expenditures under these post-2022 approvals should not include expenditures associated with the provision of non-emergency care to individuals who do not meet citizenship or immigration status requirements to be eligible for Medicaid.

DSHP Raises Oversight Concerns and Increases Federal Expenditures

Federal DSIP and DSHP funding have appeared to serve primarily as a financing mechanism for states, resulting in increased federal expenditures, rather than being an integral part of an appropriate section 1115 Medicaid demonstration. In all cases, these programs already existed at the state level and are not new Medicaid initiatives intended to test innovative approaches to promote the objectives of Medicaid. Despite the safeguards implemented in the post-2022 approvals of DSHP, CMS has renewed concerns about the same issues originally identified in 2017. DSHP represents increasing costs to the federal government without a proportional state contribution. The use of demonstration authority to match state DSHP expenditures has also historically been of concern to Congressional oversight committees and the Government Accountability Office (GAO).

In general, documentation from DSHP claiming protocols have confirmed that federal DSHP funding is neither integral to a section 1115 demonstration nor a prudent federal investment. For example, one state's approved DSHP includes grants to a labor union for the purpose of reducing the cost of providing health insurance, dental and vision benefits to certain child care providers, which does not appear integral to the state's section 1115 demonstration supporting increased access for Medicaid beneficiaries. In another state's demonstration, DSHP funds a telehealth infrastructure grant program for healthcare providers to purchase equipment, high-speed internet access, and other infrastructure.

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[1] State Medicaid Director Letter # 17-005, "Phase-out of expenditure authority for Designated State Health Programs (DSHP) in Section 1115 Demonstrations," https://www.medicaid.gov/federal-policy-guidance/downloads/smd17005.pdf.

[2] TennCare III Demonstration

[3] States with approved DSHP authority include: Arizona, California, Hawaii, Massachusetts, New York, North Carolina, Oregon, and Washington.

Next Steps
As noted earlier, CMS does not anticipate approving new state proposals for section 1115 demonstration expenditure authority for DSHP or DSIP or renewing existing section 1115 demonstration expenditure authority for DSHP or DSIP. As such, in addition to this letter, the Center for Medicaid and CHIP Services (CMCS) will conduct direct outreach to states with existing DSHP and DSIP authority to emphasize that the time-limited authority for DSHP or DSIP will not be extended beyond the currently approved demonstration period or, when current DSHP or DSIP authority concludes before the end of the demonstration's approval period, the current end date for such authority.

CMS is available to consult with states if they believe services currently supported in DSHPs and DSIPs qualify for federal matching funds under their state plans.

CMS will continue to work with states to support innovative state section 1115 demonstrations that promote the objectives of Medicaid. Questions and comments regarding this letter may be directed to Jacey Cooper, Director, State Demonstrations Group, CMCS.

Sincerely,

/s/

Drew Snyder
Deputy Administrator and Director