

Congress of the United States

Washington, DC 20510

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State Medicaid Director Tyler Sadwith
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June 24, 2026

Governor Newsom and Director Sadwith,

We are concerned by the recent passage of the State of California's Fiscal Year 2026-2027 Budget, specifically the included Managed Care Organization (MCO) tax proposal. As written, the reworked MCO tax would increase costs on commercial health plans and appears designed to preserve state revenue to offset General Fund obligations, rather than make health care more affordable.¹

Californians are already struggling with high costs of living, including rising housing costs, high gas prices, and mounting pressure on household finances for basic necessities. This proposal would place an additional financial burden on working families, employees, and employers who rely on commercial health insurance.

For years, California has exploited the MCO tax structure by concentrating the tax burden on Medicaid managed care plans, which has raised concern over compliance with federal "broad-based and uniform" tax requirements. This approach allowed the state to draw down billions in federal Medicaid funding without requiring a commensurate contribution from the state's General Fund and with minimal tax costs borne by non-Medicaid coverage. H.R. 1, the Working Families Tax Cuts Act, and the Centers for Medicare and Medicaid (CMS) updated uniformity standards which required the state to restructure the tax and restricted its ability to tax Medicaid managed care plans at substantially higher rates than commercial plans.

Before the implementation of H.R. 1, California's MCO tax rates were set at \$274 per member, per month for Medicaid, while commercial member months were taxed at \$1.75 per member, per month.² The current California tax proposal would impose a per-enrollee tax of \$8.85 per month on commercial health plans, Medicaid plans, and Affordable Care Act (ACA) Marketplace plans.³

This proposal would place an additional financial burden on working families, employees, and employers who rely on commercial health insurance. The California Legislative Analyst's Office has warned that commercial insurers will "likely recover at least some of this cost by increasing premiums on consumers,"⁴ potentially increasing health care costs for working families by hundreds of dollars each year.

¹ *THE 2026-27 BUDGET: MEDI-CAL AT THE MAY REVISION*. (n.d.). Retrieved June 16, 2026,

from <https://abgt.assembly.ca.gov/system/files/2026-05/initial-lao-analysis-of-medi-cal-at-may-revision.pdf>

² Newsom, G., & Baass, M. (n.d.). *State of California*. Retrieved June 16, 2026, from <https://www.dhcs.ca.gov/wp-content/uploads/2025/10/1903w3B-and-C-MCO-Tax-2023-2026-Amendment.pdf>

³ *THE 2026-27 BUDGET: MEDI-CAL AT THE MAY REVISION*. (n.d.). Retrieved June 16, 2026,

from <https://abgt.assembly.ca.gov/system/files/2026-05/initial-lao-analysis-of-medi-cal-at-may-revision.pdf>

⁴ *Medi-Cal Targeted Provider Rate Increases and Investments* | DHCS. (2026a, April 27). DHCS. [The 2025-26 Budget: MCO Tax and Proposition 35](#)

Rather than scaling the MCO tax rate to the lower commercial rate, the state chose to restructure the tax in a way that shifts additional costs onto commercial health plans and the enrollees they cover.

Additionally, California has historically used MCO tax revenues to offset General Fund spending, effectively freeing up General Fund resources for other state priorities. Balancing the state's budget should not come at the expense of families and individuals enrolled in commercial health plans, particularly when revenue is being directed to offset broader budget priorities rather than to make health care more affordable.


What makes this even more troubling is that Californians explicitly weighed in on this question. In November 2024, voters approved Proposition 35, which directs MCO tax revenue toward specific Medi-Cal improvements and prohibits those funds from replacing existing state Medi-Cal spending. Proposition 35 set a \$2.50 limit on commercial plans to protect Californians from premium increases.⁵ The current proposal appears to move in the opposite direction by increasing the tax on commercial plans and using the resulting revenue to support broader budget obligations.

We are concerned that the current approach does not honor Proposition 35 and ignores the will of California voters, and we respectfully request your response to the following questions:


- What is the projected cost impact on privately insured Californians under the restructured MCO tax, and what steps are being taken to mitigate those?
- How does the Administration's use of MCO tax revenue comply with Proposition 35, given that a substantial portion appears directed toward general budget stabilization?
- What share of MCO tax revenue is projected to go directly to Medi-Cal provider reimbursement rates and services?
- Has the Department analyzed alternative approaches that would limit new cost burdens on privately insured Californians? If so, we would welcome that analysis.

Our constituents deserve transparency about how this policy will affect their pocketbooks and whether it honors the commitments made to voters at the ballot box. We look forward to your prompt response. We urge the state to pursue a budget solution that does not increase health care costs for Californians, who are already struggling with California's high cost of living.

Sincerely,



Jay Obernolte
Member of Congress



Vince Fong
Member of Congress

⁵ *Medi-Cal Targeted Provider Rate Increases and Investments* | DHCS. (2026a, April 27).
DHCS. <https://www.dhcs.ca.gov/medi-cal-targeted-provider-rate-increases-and-investments/>



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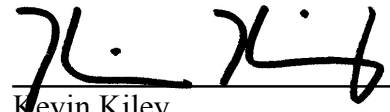
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