Explainer: CMS's Deferral, Disallowance, and Withholding Actions in Minnesota

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I. Introduction

The current administration has set forth its intention to eliminate "Fraud, Waste and Abuse" (FWA) in the Medicaid program. As part of this effort, the Centers for Medicare and Medicaid Services (CMS) has engaged in multiple drastic actions against Minnesota's Medicaid program, including initiating the process to withhold federal Medicaid funding and deferring federal reimbursement for claims the State has submitted. CMS's efforts are an unprecedented and indiscriminate attack on Minnesota's Medicaid program that have put potentially billions of dollars of federal Medicaid funding at risk. The nature of these actions, along with unclear statements from federal officials, have led to confusion as to what has already happened and what could happen to Minnesota's Medicaid funding. This explainer seeks to clarify what has already occurred and how the ongoing disputes may play out.

II. Deferral, Disallowance, and Withholding

Historically, CMS has worked collaboratively with states to identify FWA in the Medicaid program. Nevertheless, federal law provides CMS with various mechanisms to act more aggressively, in particular to deprive states of federal funding if they are not operating their Medicaid programs in accordance with federal law. CMS is using two of these mechanisms in Minnesota: the deferral and disallowance process, and the withholding process.

A. Deferral and Disallowance

CMS may refuse to provide federal financial participation (FFP), which is the funding that the federal government provides to the state for Medicaid, if an expenditure is not allowable under law. CMS accomplishes this through the "deferral and disallowance" process. The "deferral and disallowance" process is used for service claims that have already occurred and that the state has submitted to CMS for federal matching funds.

Under this process, CMS first notifies the State that it is questioning the allowability of a claim and that it needs additional information to determine if the claim should be paid.[1] The burden is then on the State to show that the claim is allowable.[2] The State has 60 days (120 days, if it requests an extension) to submit documentation to CMS to show that the claim is allowable.[3] CMS has 90 days to review the documentation and determine whether to pay or disallow the claim.[4]

If CMS disallows the claim, it must send a proper notice explaining the reasons it believes the claim is improper.[5] Within 60 days of that notice, the State may request that CMS reconsider its decision.[6] If the reconsideration is unsuccessful, the State may file an appeal with the Department of Health and Human Services' Departmental Appeals Board (DAB), which must engage in an independent and impartial review of the decision.[7] If the DAB upholds the disallowance, the State may seek judicial review of the decision in federal district court.[8]

The deferral and disallowance process is a relatively common process that CMS has employed in the past. At least 14 states have contested disallowances proposed by CMS in front of the DAB over the last five years.[9]

B. Withholding

The other process that CMS is using to deny federal funding is known as a withholding, or a compliance action. Under this process, CMS withholds future FFP because of a state's failure to substantially comply with the Medicaid Act.[10] Noncompliance may occur if a State makes an unapproved change to its Medicaid state plan or if fails to "actually comply" with federal requirements, regardless of the contents of the state

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[1] 42 C.F.R.§ 430.40(b)(1).
[2] *Id.* at § 430.40(b)(2).
[3] *Id.* at § 430.40(c)(1).
[4] *Id.* at § 430.40(c)(5).
[5] *Id.* at § 430.42(a).
[6] *Id.* at § 430.42(b). The state may also file an appeal directly to the DAB without going through the reconsideration process. *Id.* at § 430.42(b)(4).
[7] *Id.* at § 430.42(f). *But see Texas v. Brooks-LaSure*, 680 F. Supp. 3d 791, 806 (E.D. Tex. 2023) (holding that the availability of an administrative review process by the DAB did not bar Texas' claim under the Administrative Procedure Act).
[8] 42 U.S.C. § 1316(e)(2)(C).
[9] *See* Andy Schneider, Ctr. for Chil. and Fams., Georgetown Univ., *CMS Weaponize Fraud Against Medicaid in Minnesota*, (Jan. 16, 2026), **https://ccf.georgetown.edu/2026/01/16/cms-weaponizes-fraud-against-medicaid-in-minnesota/**.
[10] 42 U.S.C. § 1396c; 42 C.F.R. § 430.35(a).

plan.[11] In these circumstances, CMS may withhold all or part of the federal payments due to the State until the CMS Administrator is satisfied that the State is in compliance with federal law.[12]

Withholding of payments under this provision of law may only occur after CMS has given the State reasonable notice and opportunity for a hearing.[13] If the State files an appeal, a hearing is conducted by the CMS hearing officer under a specific set of federal regulations.[14] Following the hearing, the CMS Administrator may accept or reject the hearing officer's decision.[15] The withholding does not occur until the Administrator issues his final decision.[16] The State may appeal an adverse decision to U.S. Circuit Court of Appeals for the circuit in which the State is located.[17]

The withholding process is much less common than the deferral process.[18] The regulations themselves note that a hearing under this section is "generally not called until reasonable effort has been made to resolve the issues through conferences and discussions."[19]

III. Actions in Minnesota

The Administration has chosen to use both the deferral and disallowance process and the withholding process in Minnesota. The combined effect of these actions could deprive the State of billions of dollars of Medicaid funding.

A. January 2026 Withholding Notice

Beginning in July 2024, CMS started working with Minnesota to address fraud concerns in its Medicaid program.[20] Between July 2024 and December 2025, CMS and Minnesota

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[11] 42 C.F.R. § 430.35(b)(c).
[12] *Id.* at § 430.35(d)(2).
[13] *Id.* at § 430.35(a).
[14] *See id.* at §§ 430.60 – 430.104.
[15] *Id.* at § 430.102(b).
[16] *Id.* at § 430.35(d).
[17] *Id.* at § 430.38. That appeal may include a requirement that the adverse decision be stayed pending the conclusion of the appeal.
[18] *See* Allison Buffett et al., Bipartisan Policy Ctr., *Medicaid Payment Deferrals: What They Are and How They Work*, (Mar. 4, 2026), **https://bipartisanpolicy.org/explainer/medicaid-payment-deferrals-what-they-are-and-how-they-work/**.
[19] 42 C.F.R. § 430.35(a).
[20] *See* Notice of Opportunity for Hearing on Compliance of Minnesota State Plan Provisions Concerning Program Integrity and Fraud, Waste, and Abuse With Title XIX (Medicaid) of the Social Security Act, 91 Fed. Reg. 1539 (Jan. 14, 2026) [hereinafter "*Withholding Notice*"].

worked collaboratively to address these concerns, as is the typical process for these issues. As part of this effort, Minnesota identified 14 Medicaid services as potentially "high risk" for fraud, and eliminated one of those services from its program.[21] In response to a letter from CMS on December 5, 2025, Minnesota submitted a corrective action plan (CAP) to CMS on December 31, 2025, that outlined additional steps that Minnesota intended to take to address fraud issues in its Medicaid program.[22]

Rather than continuing to engage with the State in cooperative federalism to address fraud concerns, CMS chose to pursue an aggressive and direct attack on Minnesota's Medicaid funding. On January 6, 2026, CMS sent the State a notice of its intention to withhold millions of dollars of Medicaid funding. The notice, formally published in the Federal Register on January 14, 2026, states that "CMS has found that Minnesota's policies, practices, and oversight mechanisms violate [42 U.S.C. § 1396a(a)(64)], which requires states to ensure their state plans provide mechanisms to receive reports of alleged FWA and to compile and analyze related data."[23] CMS also concluded that "Minnesota's policies, practices, and oversight mechanisms violate federal regulations at 42 CFR Part 455, Subpart A, which require states to implement methods for identifying, investigating, and referring suspected Medicaid fraud . . . ."[24] The notice states that these findings are "the basis for withholding federal financial participation (FFP) from Minnesota's Medicaid program" and that "[t]he withholding will end when the Minnesota Medicaid agency fully and satisfactorily implements a corrective action plan (CAP) to bring its program integrity operations into compliance with federal requirements."[25] CMS estimated the withholding amount to be approximately $515 million per quarter, or $2 billion per year, which is based on "the federal share for one quarter's amount of the previous calendar year's annual total paid expenditures for the fourteen high-risk services."[26]

In addition, the notice explained that CMS intended to "take additional steps . . . to conduct reviews of state expenditures" of the 14 Medicaid services identified by the State. The notice stated that "CMS intends to issue deferral or disallowance of any FFP claimed by the state that does not meet applicable federal requirements."[27] The review process appeared to occur over the months of January and February 2026, leading to a second notice at the end of February.

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[21] *Id.*
[22] *Id.*
[23] *Id.*
[24] *Id.*
[25] *Id.*
[26] *Id.* at 1542.
[27] *Id.*

B. February 2026 Deferral Notice

On February 25, 2026, CMS provided notice to Minnesota "of four deferrals totaling $259,505,491 federal financial participation (FFP)" for "expenditures claimed on Form CMS-64 for the quarter ending September 30, 2025, certified on December 30, 2025."[28] CMS deferred approximately $15.4 million in Medicaid expenditures for services to "individuals lacking a satisfactory immigration status" and approximately $243.8 million in claims related to the 14 "high-risk" Medicaid services.[29] Of the $243.8 million, approximately $164 million involve claims from "other practitioner, personal care, and home and community-based services lines that have questionable variances and raise concerns about allowability of the claimed expenditures," while approximately $79.5 million involve claims "submitted to the state by specific providers that CMS have identified as high-risk for fraud or aberrant billing practices."[30] Thus, it appears that the deferral may be an attempt to work around the withhold process and allow CMS to divest the State of funding without delay. In accordance with federal regulations, Minnesota was given 60 days to provide documents and materials so that CMS can "make a proper determination on the allowability of the claim."[31]

The February 25, 2026, deferral notice is highly unusual for multiple reasons. First, the deferral that Minnesota faces is much larger in amount and scope than other deferrals that CMS has issued in the past. According to the Center on Budget and Policy Priorities' review of decisions of the DAB over the past 10 years, "the deferral amounts leading to disallowances ranged from $2.4 million to $43.7 million."[32] In addition, the deferrals are typically targeted to instances where there is a question of whether a particular claim is allowable under Medicaid, and detailed notice is often provided to the state Medicaid agency on what additional documentation is needed. In this instance, CMS is targeting a broad array of services that Minnesota previously identified, and the only rationale it

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[28] *See* Letter from Dorothy Ferguson, Dir., Div. of Fin. Operations W., Ctr. for Medicaid & CHIP Servs., to John Connolly, State Medicaid Dir., Minn. Dep't of Hum. Servs., (Feb. 25, 2026), **https://www.documentcloud.org/documents/27420090-cms-medicaid-deferral-letter-q4-2025/**) [hereinafter "*Deferral Notice*"].

[29] *Id.*

[30] *Id.*

[31] *Id.*

[32] *See* Andy Schneider, Ctr. for Chil. and Fams., Georgetown Univ., *CMS Weaponize Fraud Against Medicaid in Minnesota: Part 2*, (Mar. 2, 2026), **https://ccf.georgetown.edu/2026/03/02/cms-weaponizes-fraud-against-medicaid-in-minnesota-part-2/**.

has provided to support the deferral is that the claims at issue have "questionable variances" or are from providers who CMS has "identified as high-risk for fraud."[33]

C. Next Steps

As noted above, both the withholding and deferral and disallowance processes allow states to challenge CMS's determinations, and Minnesota will do so. On January 9, 2026, Minnesota filed an administrative appeal of the January 6, 2026, withholding notice.[34] As of this writing, an appeal hearing has not been scheduled. The regulations governing the appeal process give parties "the right to conduct discovery (including depositions) against opposing parties."[35] We understand that Minnesota does plan to conduct discovery, so it is likely that a hearing may not occur for several months.

With respect to the deferral and disallowance process, Minnesota has until April 26, 2026, to submit its documentation to dispute CMS's claims regarding unallowable expenses. Assuming all documentation is in a reviewable form, CMS would then have until July 25, 2026, to determine the allowability of the claim. This timeline could be delayed if Minnesota requests an extension or if CMS determines that the documentation is not in a reviewable form. If CMS decides to issue disallowances following its review of the documentation, the reconsideration process would push into the later part of 2026, with an appeal to the DAB and potentially further appeal to federal district court to follow.

Minnesota is also challenging the deferral action through affirmative litigation in federal court. On March 2, 2026, the State filed a lawsuit in the U.S. District Court of Minnesota against CMS, HHS, and the heads of both agencies, alleging that the deferral action violates numerous provisions of federal law.[36] Specifically, Minnesota has asserted that the Defendants have violated the procedural due process requirements of the Fifth Amendment, the Administrative Procedure Act, the Spending Clause, and that the action was ultra vires.[37] Minnesota has filed a motion for a Temporary Restraining Order (TRO), which asks the court to enjoin Defendants from immediately deferring over $243

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[33] *See Deferral Notice*.
[34] *See* Letter from John Connolly, State Medicaid Dir., Minn. Dep't of Human Servs. to Mehmet Oz, M.D., Adm'r, Center for Medicaid & Medicare Servs., (Jan. 9, 2026), **https://interactive.kare11.com/pdfs/DHS-appeal-to-CMS-action.pdf**.
[35] 42 C.F.R. § 430.86
[36] Compl., *State of Minn. et al. v. Dr. Mehmet Oz et al.*, 26-cv-01701 (D. Minn., Mar. 2, 2026), **https://www.ag.state.mn.us/Office/Communications/2026/docs/01701_Oz_Complaint.pdf**.
[37] *Id.*

million in Medicaid funding. The TRO motion will be heard on March 12 and is likely to be decided quickly.

It is possible that CMS and Minnesota could resolve the withholding and deferral (and potential disallowance) with a CAP. Minnesota submitted a revised CAP to CMS at the end of January 2026, which is currently under review. The withholding notice explains that the "withholding will end when the Minnesota Medicaid agency fully and satisfactorily implements a corrective action plan (CAP)."[38] Therefore, if CMS accepts Minnesota's revised CAP, the withholding process will presumably not go forward. It is less clear whether a CAP would also resolve the deferral, as CMS could still pursue disallowances even if Minnesota has an acceptable CAP in place.

One crucial question is when exactly Minnesota will be deprived of FFP. The withholding process cannot go forward until CMS has provided Minnesota with a hearing and issued a final decision, and thus the $515 million quarterly withholding should not occur for several months.

However, the deferral process results in an immediate delay of FFP to Minnesota. If CMS determines not to go forward with the disallowance process, Minnesota will eventually receive FFP for the quarter ending September 30, 2025, although it is difficult to estimate exactly when that would occur. However, if CMS decides to move forward with a disallowance and the federal court does not grant Minnesota's request for an injunction in its affirmative litigation to stop the process, Minnesota will not receive the FFP for the quarter ending September 30, 2025, unless the state is successful in the reconsideration, DAB, or federal court appeal processes. In that circumstance, it could be months, or potentially years, before Minnesota receives FFP for those service claims if it is ultimately successful on appeal.

IV. Conclusion

The actions that the administration has taken against Minnesota's Medicaid program are unprecedented in scope and have the potential to severely disrupt the provision of Medicaid services to Minnesotans. Significantly, Minnesota is not the only state being targeted by the administration, which has indicated that it plans to take similar actions against other states. Indeed, several states have already been targeted, with California, Maine, and New York having received letters from CMS raising concerns with FWA in the operation of their Medicaid programs. As in Minnesota, the same or similar home and community-based, behavioral health, and transportation services are targeted. Consequently, advocates should continue to pay attention to CMS's actions toward Minnesota, as they could have ripple effects for Medicaid programs across the country.

[38] *See Withholding Notice.*