

Cite as Det. No. 15-0088, 34 WTD 524 (2015)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petitions for Refund of)	<u>D E T E R M I N A T I O N</u>
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)	No. 15-0088
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[1] RCW 82.04.290(2); RCW 82.04.4286: SERVICE B&O TAX – FEDERAL PREEMPTION – FEDERAL EMPLOYEES HEALTH BENEFITS ACT (FEHBA) – 5 USC § 8909(f)(1) – HEALTH CARE PROVIDER’S RECEIPTS FROM FEHBA INSURANCE CARRIERS. Service B&O tax imposed on a health care provider’s receipts from insurance carriers who participate in the FEHB program is not a direct or indirect tax imposed on a FEHBA carrier with respect to payments made from the FEHB fund and, therefore, is not preempted by 5 USC § 8909(f)(1).

[2] RCW 82.04.290(2); RCW 82.04.4286: SERVICE B&O TAX – FEDERAL PREEMPTION – 42 CFR § 422.404 – HEALTH CARE PROVIDER’S RECEIPTS FROM MEDICARE ADVANTAGE (MA) PLANS. Service B&O tax imposed on a health care provider’s receipts from MA Plans is not a tax imposed on payments Centers for Medicare & Medicaid Services makes on behalf of MA enrollees to MA Plans and, therefore, is not preempted by 42 CFR § 422.404.

[3] RCW 82.04.290(2); RCW 82.04.4286: SERVICE B&O TAX – FEDERAL PREEMPTION – 10 USC § 1103(a) – 32 CFR § 199.17(a)(7) – HEALTH CARE PROVIDER’S RECEIPTS FROM TRICARE INSURANCE CARRIERS. Service B&O tax imposed on a health care provider’s receipts from TRICARE insurance carriers, pursuant to RCW 82.04.290, is not a tax imposed on the premiums or other payments that TRICARE insurance carriers receive from the TRICARE program; therefore, the tax is not preempted pursuant 10 USC § 1103(a) and 32 CFR § 199.17(a)(7).

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

Sohng, A.L.J. – Health care providers appeal the denials of their requests for refund of business and occupation [(“B&O”)] tax paid on receipts from insurance carriers that participate in federal health insurance programs, asserting that Washington’s tax is preempted by federal law. Taxpayers’ petitions are denied.¹

ISSUES

1. Whether the imposition of [B&O] tax on health care provider’s receipts from insurance carriers who participate in the Federal Employee Health Benefits (“FEHB”) program is preempted by 5 USC § 8909(f).
2. Whether the imposition of [B&O] tax on health care provider’s receipts from insurance carriers who participate in the Medicare Advantage [(“MA”)] program are preempted by 42 CFR § 422.404.
3. Whether the imposition of [B&O] tax on health care provider’s receipts from insurance carriers who participate in the TRICARE program are preempted by 32 CFR § 199.17(a)(7).

FINDINGS OF FACT

This appeal involves two related entities: [Taxpayers]. Taxpayers are [for-profit] Washington corporations engaged in the business of providing home health and home care services in this state. On December 30, 2013, [Taxpayers] each submitted refund claims to the Department of Revenue (“Department”) in the amounts of \$. . . and \$. . . , respectively, for the period January 2009 through December 2012 (the “Refund Period”). The basis for Taxpayers’ claims is that Taxpayers are not subject to Washington’s [B&O] taxes under the federal preemption doctrine on payments they receive from the three federally funded healthcare plans described below. On February 19, 2014, the Department denied Taxpayers’ refund claims on the grounds that federal preemption doctrine did not apply to payments made to health care providers from these three plans. Taxpayers appeal the refund denials.

The Federal Employees Health Benefits Act of 1959 (“FEHBA”) establishes a comprehensive program of health insurance for civilian employees of the federal government, their dependents, and federal retirees. 5 USC § 8901 *et seq.* FEHBA authorizes the Office of Personnel Management to contract with private insurance carriers to offer federal employees an array of health care plans. 5 USC § 8902(a). To purchase insurance under a FEHBA plan, enrollees make payments, matched by contributions from the federal government, into a specifically designated account in the United State Treasury, entitled the Federal Employees Health Benefits Fund (the “FEHB Fund”). 5 USC §§ 8906, 8909. Insurance carriers pay Taxpayers by drawing against the FEHB Fund to pay for covered health care benefits. *Id.*; *see also* 48 CFR § 1632.170(b). Taxpayers do not provide group insurance policies or similar arrangements in consideration of premiums or other periodic charges.

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

[MA] is a type of Medicare health plan under which the federal government pays a private insurance company to take over coverage for a Medicare eligible individual. The private insurance company contracts with the Centers for Medicare & Medicaid Services (“CMS”), a federal agency, to provide Medicare benefits. *See* 42 CFR § 422.2. Taxpayers do not receive any payments from CMS or other Medicare funds; rather, Taxpayers receive payments from MA plans for health services provided to their patients who are MA enrollees.

TRICARE provides a comprehensive managed health care program for active and retired military personnel and their dependents. The United States Department of Defense administers the TRICARE program. 32 CFR § 199.17(a).

Taxpayers received payments from insurance carriers under the three federal programs above during the Refund Period. They argue that the State of Washington is specifically preempted from taxing receipts from these sources.

ANALYSIS

RCW 82.04.220 imposes the [B&O] tax “for the act or privilege of engaging in business activities.” Persons, such as Taxpayers, who are engaged in a service business or business that is not specifically taxed under another B&O tax classification, are generally required to pay B&O tax under RCW 82.04.290(2), measured by the “gross income of the business.”

The Supremacy Clause of the United States Constitution provides that the Constitution and federal laws are the supreme law of the land.² U.S. CONST., ART. VI., cl.2. Federal law can preempt state law through: (1) express preemption; (2) field preemption (sometimes referred to as complete preemption); and (3) conflict preemption. *Int’l Paper Co. v. Ouellette*, 479 U.S. 481, 491, 107 S.Ct. 805 (1987). Express preemption exists where Congress enacts an explicit statutory mandate that state law be displaced. *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 382, 112 S.Ct. 2031 (1992). Absent explicit preemptive text, preemption may be inferred based on field or conflict preemption, both of which require us to [infer] Congress’ intent from the statute’s structure and purpose. *FMC Corp. v. Holliday*, 498 U.S. 52, 56-57, 111 S.Ct. 403 (1990).

When considering preemption, no matter which type, “the purpose of Congress is the ultimate touchstone.” *Cipollene v. Liggett Group, Inc.*, 505 U.S. 504, 516, 112 S.Ct. 2608 (1992); *New York State Conference of Blue Cross & Blue Shiled Plans v. Travelers Ins. Co.*, 514 U.S. 645, 655, 115 S.Ct. 1671 (1995). In order to avoid an unintended encroachment on state authority, the Supreme Court has made clear that when interpreting a federal statute, courts should be reluctant to find preemption. *CSX Transportation v. Easterwood*, 507 U.S. 658, 662-64, 113 S.Ct. 1671 (1995); *Travelers*, 514 U.S. at 654. Evidence of pre-emptive purpose is sought in the text and structure of the statute at issue. *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 95, 103 S.Ct. 2890

² RCW 82.04.4286 provides, “In computing tax there may be deducted from the measure of tax amounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States.”]

(1983). “If the statute contains an express pre-emption clause, the task of statutory construction must in the first instance focus on the plain wording of the clause, which necessarily contains the best evidence of Congress' pre-emptive intent.” *CSX*, 507 U.S. at 664.

. . . . The preemption provisions for the three federal programs are each provided below.

1. FEHB Program

FEHBA contains the following preemption provision forbidding states from taxing health insurance carriers with respect to payments made to them from the FEHB Fund:

No tax, fee, or other monetary payment may be imposed, directly or indirectly, on a carrier or an underwriting or plan administration subcontractor of an approved health benefits plan by any State, . . . with respect to any payment made from the [FEHB] Fund.

5 USC § 8909(f)(1)(emphasis added). FEHBA defines a “carrier” as:

A voluntary association, corporation, partnership, or other nongovernmental organization which is lawfully engaged in providing, paying for, or reimbursing the cost of, health services under group insurance policies or contracts, medical or hospital service agreements, membership or subscription contracts, or similar group arrangements, in consideration of premiums or other periodic charges payable to the carrier, including a health benefits plan duly sponsored or underwritten by an employee organization and an association of organizations or other entities described in this paragraph sponsoring a health benefits plan.

5 USC § 8901(7) (emphasis added.).

The Washington Court of Appeals reviewed the FEHBA preemption provision cited above in relation to Seattle’s B&O tax in *Group Health Cooperative v. City Seattle*, 146 Wn. App. 80, 189 P.3d 216 (2008). The court set forth the established requirements to invoke the preemption doctrine:

Under 5 USC § 8909(f)(1), state regulation is preempted if it is (1) a state or local tax, fee, or other monetary payment; (2) imposed directly or indirectly on a carrier; and (3) with respect to payments made from the [FEHB Fund].” *Health Maint. Org. of N.[J]., Inc. v. Whitman*, 72 F.3d 1123, 1128 (3rd Cir. 1995).

Group Health, 146 Wn. App. at 94 (bracketed term ours).

In that case, Group Health Cooperative, a health maintenance organization (“HMO”), received premium payments from its patient members in exchange for health services, and received premium payments made by the federal government from the FEHB Fund for those patients that are covered by the FEHB program. *Id.* at 83-84. The court held that Group Health was a *carrier*, as defined by the FEHBA, that contracted with the federal government to provide health care coverage in exchange for payments from the FEHB Fund; therefore, the court concluded that 5

USC § 8909(f)(1) preempted the city's imposition of B&O tax on Group Health's receipts from the FEHB Fund. *Group Health*, 146 Wn. App. at 95-96.

The circumstances in the present appeal are entirely different from those in *Group Health*. Here, Taxpayers are not "carriers" under 5 USC § 8909 because [they] do not provide group insurance policies or similar arrangements in exchange for premiums or other periodic dues. Moreover, Taxpayers do not receive payments from the FEHB Fund; therefore, the FEHBA preemption provision does not apply to them under the [plain] language of 5 USC § 8909(f)(1).

Taxpayers' argument on appeal is based on an economic pass-through theory: that the imposition of Washington's B&O tax on its gross receipts from FEHBA insurance carriers is a tax imposed *indirectly* on the FEHBA carrier's receipts from the FEHB Fund because Taxpayers may pass along their tax costs to the carriers in setting the charges for their services. Arguments based on similar economic pass-through theories were made by the federal government in *United States v. West Virginia*, 339 F.3d 212 (4th Cir. 1995), and more recently by a medical products retailer in *Mobility Medical, Inc. v. Mississippi Dep't of Revenue*, 119 So. 3d 1002 (2013). The courts in both cases held that taxing the gross income of a business that receives payments from a FEHBA carrier was not an indirect imposition of a tax on a FEHBA carrier with respect to payments from the FEHB Fund. *West Virginia*, 339 F.3d at 218-219; *Mobility Medical*, 119 So. 3d at 1005.

In *West Virginia*, the Fourth Circuit held that even though health care providers *could* pass the economic costs of a gross receipts tax to an insurance carrier, that potential choice by the providers did not constitute a prohibited imposition of an indirect tax on the insurance carrier. *West Virginia*, 339 F.3d at 218-219. The court stated that the legal [incidence] of the state gross receipts tax fell on the providers alone and a possible economic pass-through of costs to FEHBA carriers does not equate to the indirect imposition of a tax.³ *Id.* In further support of its holding, the court relied on the Supreme Court's rejection of economic pass-through theories in determining what constitutes indirect taxation in the analogous constitutional field of preemption of state taxation of the federal government. *Id.* at 216 (*citing United States v. Fresno*, 429 U.S. 452, 459, 97 S.Ct. 699 (1977) (state taxation of federal employees' housing benefit, though passing an economic burden through to the federal government by lowering the effective pay rate of its employees, was not a prohibited tax on the federal government because the tax equally applied to other similarly situated constituents of the state)). The *West Virginia* court determined that the rule espoused by the *Fresno* Court should also apply to the FEHBA preemption provision because of the similarities between the prohibitions:

Fresno's holding therefore results in the rule that an economic pass-through of a generally applicable tax does not constitute a tax, direct or indirect, of the recipient of the pass-through. . . .

³The Fourth Circuit did not find helpful the federal government's citation to Office of Personnel Management regulation 48 CFR § 1631.205-41, which provides, in part: "5 USC § 8909(f)(1) prohibits the imposition of taxes . . ., directly or indirectly, on FEHB premiums . . . and it applies to all forms of direct and indirect measurements of FEHBP premiums . . . regardless of how they may be titled, to whom they must be paid, or the purpose for which they are collected . . ." *West Virginia*, 339 F.3d at 214, fn 1. The court stated, "this regulatory instruction, saying nothing about from whom the tax is collected, sheds no light on what constitutes indirectness, as such relates to the relationship between a tax and its payer." *Id.*

Fresno's rule should apply here by analogy because of the many similarities between section 8909(f)'s preemption and the Constitution's preemption of state taxation of the federal government. Section 8909(f) precludes states from taxing the Carriers directly or indirectly. The Constitution precludes states from taxing the federal government directly or indirectly. Both ensure that state tax laws do not thwart the will of the federal government. Both face the economic reality that the states' tax regimes would be seriously hampered were all state taxes of non-protected taxpayers that create pass-through economic burdens on protected taxpayers treated as indirect taxes of those protected taxpayers.

West Virginia, 339 F.3d at 216-217.

The Mississippi Supreme Court also refused to equate a potential economic pass-through of costs to an indirect tax on FEHBA carriers in *Mobility Medical, Inc. v. Mississippi Dep't of Revenue*, 119 So.3d 1002 (2013). *Mobility Medical*, a medical products retailer, asserted that FEHBA preempted Mississippi's gross receipts tax on its revenues from FEHBA carriers because any state tax that *might* result in an increase in costs for the FEHB Fund is an indirect tax. *Mobility Medical*, 119 So. 2d, at 1004-1005. The court held that nothing in the Mississippi tax law requires the retailer to pass on the tax (or any of its costs) to its customers, or that the retailer be reimbursed its costs by the FEHB Fund; therefore, there was no preemption because there was no indirect tax on the carrier, or conflict between the state and federal laws. *Id.* The court noted that if an economic cost "trickle-down effect" amounted to an indirect tax, then preemption would equally apply to all state and local taxes born by any retailer, including inventory tax, unemployment tax, property taxes, franchise tax, license fees, and the numerous taxes or fees that a retailer might "indirectly" pass along to its customers, and that there was no evidence of such expansive Congressional intent in the FEHBA. *Id.*

Taxpayers' reliance on *Health Maint. Org. of New Jersey v. Whitman*, 72 F.3d 1123, 1125 (3rd Cir. 1993), and *Travelers Ins. Co. v. Cuomo*, 14 F.3d 708, 716 (2d Cir. 1993) is misplaced, as both cases involve the preemption of a tax on a FEHBA carrier.⁴ In *Whitman*, the imposition was levied by the state on the carriers as a direct special assessment, and in *Travelers*, the imposition was levied by the hospital on the carriers, under the state's dictate, as a surcharge added to invoices paid by the carriers. *Whitman*, 72 F.3d at 1125; *Travelers*, 14 F.3d at 716⁵; see *West Virginia*, 339 F.3d at 217.

Taxpayer also cites to a Minnesota Tax Court decision, *Health Partners, Inc. v. Comm'r of Revenue*, No. 6925, 1999 WL 123289 . . . (Minn. Tax March 4, 1999), that involved Minnesota's gross revenues tax on hospitals and health care providers. The Minnesota Tax Court determined that FEHBA preempted the state tax as applied to HealthPartners, Inc., an HMO and FEHBA

⁴ See Supplemental Appeal Petition supplement, at 8-10 (Aug. 20, 2014).

⁵ In *Travelers*, the court found that New York's hospital surcharge was preempted by both the FEHBA and the Employee Retirement Income Security Act (ERISA). *Travelers*, 14 F.3d at 725. The Supreme Court granted certiorari solely in regards to the Second Circuit's holding that the ERISA preempted New York's hospital surcharge, and reversed, holding that the surcharges only indirectly affected the relative prices of insurance policies and Congress could not possibly have intended to eliminate the myriad of state and local regulation that could have such an indirect affect on price. *New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 668, 115 S.Ct. 1671, 131 L.Ed.2d 695 (1995).

carrier, because the tax on a carrier's gross revenues amounted to an indirect tax on the carrier with respect to payments from the FEHB Fund, a holding along the same lines as the holding in *Group Health, supra. Health Partners*, 1999 WL 123289, at *6. The Minnesota Tax Court emphasized the significance of the fact that the taxpayer was an HMO, and therefore, a carrier as well as a health service provider, just as the *Group Health* Court emphasized Group Health's HMO/carrier status. *Health Partners*, 1999 WL 123289, at *6-7; *Group Health*, 146 Wn. App. at 95.

As recognized by the above authorities, 5 USC § 8909(f)(1) limits preemption to taxes "imposed, directly or indirectly, on a carrier," and this limitation is clearly expressed in the plain language of that preemption provision. *See also* Det. No. 13-0240, 33 WTD 354 (2014). We need look no further than the plain language of the preemption provision in discerning Congress's intent. *See CSX*, 507 U.S. at 664. Taxpayers have not established that Washington's B&O tax on their gross revenues as health service providers is a direct or indirect tax imposed on a FEHBA carrier that is preempted by 5 USC § 8909(f)(1). *See also* Det. No. 13-0240, 33 WTD 354 (2014).

2. Medicare Advantage Program

Taxpayers assert that Washington's B&O tax on their gross revenues received from insurance carriers who receive payments from the [MA] program is preempted by 42 CFR § 422.404, which provides:

§ 422.404 State premium taxes prohibited.

(a) Basic rule. No premium tax, fee, or other similar assessment may be imposed by any State, . . . with respect to any payment CMS makes on behalf of MA enrollees under subpart G of this part, or with respect to any payment made to MA plans by beneficiaries, or payment to MA plans by a third party on a beneficiary's behalf.

(b) Construction. Nothing in this section shall be construed to exempt any MA organization from taxes, fees, or other monetary assessments related to the net income or profit that accrues to, or is realized by, the organization from business conducted under this part, if that tax, fee, or payment is applicable to a broad range of business activity.

(Emphasis added.) The terms "MA organization" and "MA plan" are defined in 42 CFR 422.2 as follows:

MA organization means a public or private entity organized and licensed by a State as a risk-bearing entity (with the exception of provider-sponsored organizations receiving waivers) that is certified by [Center for Medicare & Medicaid Services ("CMS")] as meeting the MA contract requirements.

MA plan means health benefits coverage offered under a policy or contract by an MA organization that includes a specific set of health benefits offered at a uniform premium and uniform level cost-sharing to all Medicare beneficiaries residing in the service area of the MA plan

(Emphasis added.) Similar to the FEHBA preemption provision, 42 CFR 422.404 is limited to taxing payments made by CMS from the federal fund [to MA plans]. Taxpayers are not MA plans or MA organizations because they are not risk-bearing entities and do not receive any payments from CMS or the Medicare fund. Taxpayers receive payments from MA plans for health services provided to their patients who are MA enrollees. Washington's B&O tax on Taxpayers' gross receipts from health services is not a [premium] tax or other assessment imposed "with respect to any payment CMS makes on behalf of MA enrollees . . . or any payment made to MA plans . . ." and is not prohibited by 42 CFR 422.404(a). Taxpayers' economic pass-through argument that their tax costs may be passed along to MA plans does not amount to a prohibited tax or assessment under the same analysis of *Fresno*, *West Virginia*, and *Medical Mobility* discussed above in regards to preemption under FEHBA.

3. TRICARE Program

Taxpayers assert that Washington's B&O tax on their gross revenues from carriers who receive payments from the TRICARE program is preempted by 32 CFR § 199.17(a)(7), which provides:

(ii) . . . any State or local law relating to health insurance, prepaid health plans, or other health care delivery or financing methods is preempted and does not apply in connection with TRICARE regional contracts. Any such law, or regulation pursuant to such law, is without any force or effect, and State or local governments have no legal authority to enforce them in relation to the TRICARE regional contracts. . . .

(iii) The preemption of State and local laws set forth in paragraph (a)(7)(ii) of this section includes State and local laws imposing premium taxes on health or dental insurance carriers or underwriters or other plan managers, or similar taxes on such entities. . . . For purposes of assessing the effect of Federal preemption of State and local taxes and fees in connection with DoD health and dental services contracts, interpretations shall be consistent with those applicable to the Federal Employees Health Benefits Program under 5 USC § 8909(f).

(Emphasis added.) *See* 10 USC § 1103(a).⁶

Preemption is limited to state and local laws relating to [health insurance or other health care delivery or financing, including] premium taxes imposed on the insurance [carriers who contract with the Department of Defense]. Washington's B&O tax [is not related to health insurance or health care delivery or financing, and it] is imposed on Taxpayers' receipts *from* insurance

⁶ The statutory preemption provision in 10 USC § 1103(a) provides:

(a) Occurrence of preemption. A law or regulation of a State or local government relating to health insurance, prepaid health plans, or other health care delivery or financing methods shall not apply to any contract entered into pursuant to this chapter by the Secretary of Defense or the administering Secretaries to the extent that the Secretary of Defense or the administering Secretaries determine that:

(1) the State or local law or regulation is inconsistent with a specific provision of the contract or a regulation promulgated by the Secretary of Defense or the administering Secretaries pursuant to this chapter; or

(2) the preemption of the State or local law or regulation is necessary to implement or administer the provisions of the contract or to achieve any other important Federal interest.

carriers, not on the premiums or other payments the insurance carriers may receive from the TRICARE program. Taxpayers have not established that Washington's B&O tax on their receipts from TRICARE [carriers] is preempted pursuant to 32 CFR § 199.17(a)(7). Their economic pass-through theory of preemption fails under the same analysis applied to the FEHBA preemption provision above. *See also* Det. No. 13-0240, 33 WTD 354 (2014). Taxpayers' petitions are denied.

DECISION AND DISPOSITION

Taxpayers' refund petitions are denied.

Dated this 7th day of April, 2015.