

Cite as Det. No. 14-0344, 34 WTD 288 (2015)

BEFORE THE APPEALS DIVISION  
 DEPARTMENT OF REVENUE  
 STATE OF WASHINGTON

In the Matter of the Petition for Refund of	)	<u>D E T E R M I N A T I O N</u>
	)	
	)	No. 14-0344
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...	)	Registration No. . . .
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...	)	Registration No. . . .
	)	

[1] RCW 82.04.4311: B&O TAX – NONPROFIT HOSPITAL -- MEDICAID & CHIP EXEMPTION. Out of state Medicaid and CHIP payments to a nonprofit hospital are not exempt from B&O tax.

[2] RCW 82.04.4297: B&O TAX -- FEDERAL MEDICAID CONTRIBUTION. A nonprofit hospital may not deduct the Federal Medicaid contribution to another state from its Medicaid payments to measure its B&O tax.

[3] RULE 201: B&O TAX – HOSPITAL – EMPLOYEES – INTERDEPARTMENTAL CHARGES. A hospital may not deduct payments to its self-insured medical plan for medical services that it provided to its employees.

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.

M. Pree, A.L.J. – Two [out of state] nonprofit hospitals seek a refund of business and occupation (B&O) tax paid on . . . Medicaid payments and . . . Children’s Health Insurance Program (CHIP) for medical care provided in Washington. They also seek a refund of B&O tax on medical services that they provided to their employees covered by the hospitals’ self-insurance plans. Because no exclusion applies to payments from . . . Medicaid and CHIP, and the medical services provided to the hospitals’ employees were taxable activities, we deny their petitions.<sup>1</sup>

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

## ISSUES

1. Under RCW 82.04.4311, may nonprofit hospitals exclude [out of state]. . . Medicaid and [out of state]. . . CHIP payments from their measure of B&O tax?
2. If the [out of state]. . . Medicaid and CHIP payments are not excludable under RCW 82.04.4311, may the hospitals exclude the federal contributions to [the state] for the Medicaid services from the B&O tax under RCW 82.04.4297?
3. Under WAC 458-20-201 (Rule 201), may hospitals exclude payments from their measure of B&O tax for medical services that they provide to their employees when the payments are from their trust accounts for their self-insured medical services plans?

## FINDINGS OF FACT

[Taxpayers] are two nonprofit medical centers providing health care services. They operate two hospitals and clinics in Washington. They receive payments from [out of state] for medical services that they provide to [out of state] residents covered by Medicaid and CHIP. The taxpayers also provide services for their employees covered by the taxpayers' self-insurance medical plan.

The taxpayers applied for a refund from the Department of Revenue (Department) for the period from December 1, 2007 through December 31, 2008. The Department's Audit Division reviewed the refund request, and allowed it in part, and denied it in part. The taxpayers appealed the refund denials. \$. . . in B&O tax is in dispute.

The taxpayers have identified two issues. First, they contend . . . Medicaid and . . . CHIP payments should be deducted from the measure of B&O tax. Second, the taxpayers contend that payments from their medical plan trust account for medical services that they provided to their employees should be exempt from B&O tax as interdepartmental charges.

One of the taxpayers' hospitals is [near] Washington's . . . border and serves many [out of state] patients. The [other] state . . . pays the taxpayers for medical services covered by [the other state's]. . . Medicaid program and CHIP. Medicaid provides health coverage for some low-income people, families and children, pregnant women, the elderly, and people with disabilities. CHIP provides health coverage to children in families that have incomes too high to qualify for Medicaid, but cannot afford private coverage. Medicaid and CHIP are administered by the states, but jointly funded by the federal government and states. *See* 42 CFR §430. The taxpayers paid B&O tax on the [the other state's]. . . Medicaid and CHIP payments, and seek to have the B&O tax refunded. In the alternative, the taxpayers seek to have the federal portion of Medicaid and CHIP payments refunded.<sup>2</sup>

The taxpayers maintain a self-insured medical plan to cover the costs of their employees. As the taxpayers compensate their employees for their work, the taxpayers pay money into a trust account administered by an independent fiduciary. When employees incur medical costs for

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<sup>2</sup> The applicable percentages are set by the Department of Health and Human Services and can be found at <http://aspe.hhs.gov/health/reports/2014/FMAP2015/fmap15.cfm> (last visited October 10, 2014).

services covered under the taxpayers' plan, money is drawn from the account either to pay third party providers or the taxpayers. The taxpayers contend that the funds for services they provide are merely transferred from one of their accounts to another bank account that they control "in order to ease the compliance burden associated with Medicare reporting requirements."<sup>3</sup>

### ANALYSIS

The B&O tax is imposed for the privilege of engaging in business in Washington. RCW 82.04.220. The term "business" includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or another person or class, directly or indirectly." RCW 82.04.140. The legislature intended to impose the B&O tax on virtually all business activities carried on within the state. *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971). The taxpayers' medical services in Washington constitute engaging in business.

The measure of B&O tax is the gross proceeds of sales, or the gross income of the business. RCW 82.04.220. RCW 82.04.080 defines "gross income of the business:"

"Gross income of the business" means the value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation for the rendition of services, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

The taxpayers seek a deduction from its gross income . . . under RCW 82.04.4311, which provides in subsection (1):

A public hospital that is owned by a municipal corporation or political subdivision, or a nonprofit hospital, or a nonprofit community health center, or a network of nonprofit community health centers, that qualifies as a health and social welfare organization as defined in RCW 82.04.431, may deduct from the measure of tax amounts received as compensation for health care services covered under the federal medicare program authorized under Title XVIII of the federal social security act; medical assistance, children's health, or other program under chapter 74.09 RCW; or for the state of Washington basic health plan under chapter 70.47 RCW. The deduction authorized by this section does not apply to amounts received from patient copayments or patient deductibles.

As a nonprofit hospital, the Audit Division recognized that the taxpayers could deduct federal Medicare payments and Washington State Medicaid payments. Our first issue is whether the taxpayers could deduct [out of state] Medicaid payments. RCW 82.04.4311(1) limits the deduction to "compensation for health care services covered under:"

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<sup>3</sup> From taxpayers' post hearing letter, dated Oct. 3, 2014.

- (1) “The federal Medicare program authorized under Title XVIII of the federal social security act;”
- (2) “Medical assistance, children’s health, or other program under chapter 74.09 RCW;”  
or
- (3) “For the state of Washington basic health plan under chapter 70.47 RCW.”

The taxpayers’ [out of state] Medicaid and [out of state] CHIP receipts are not from any of these programs. The taxpayers argue that the second phrase, “medical assistance, children’s health, or other program under chapter 74.09 RCW;” should apply to Medicaid payments from all states as well as CHIP payments. We must determine whether that second phrase applies only to Medicaid and CHIP payments from Washington, or whether Medicaid and CHIP payments from other states are also included in these medical programs under chapter 74.09 RCW.

The goal of interpreting a statute is to carry out the intent of the legislature. *Lake v. Woodcreek Homeowners Ass’n*, 169 Wn.2d 516, 526, 243 P.3d 1283 (2010). Statutory interpretation begins with the statute’s plain meaning. *Id.* The statute’s plain meaning is discerned from the ordinary meaning of the language at issue, the statute’s context, related provisions, and the statutory scheme as a whole. *Id.* The “plain meaning” of a statutory provision is to be discerned from the ordinary meaning of the language at issue, as well as from the context of the statute in which that provision is found, related provisions, and the statutory scheme as a whole. *Wash. Pub. Ports Ass’n v. Dep’t of Revenue*, 148 Wn.2d 637, 645, 62 P.3d 462 (2003); *Dep’t of Ecology v. Campbell & Gwinn L.L.C.*, 146 Wn.2d 1, 10-12, 43 P.3d 4, 9 (2002).

Examining the plain meaning of this text, all these terms must be read together. Thus, only payments covered by the medical assistance program or children’s health program (or other program) authorized under chapter 74.09 RCW are exempt from taxation. Chapter 74.09 RCW refers to Washington’s codification of the federal Medicaid and CHIP programs. See 74.09.010(1) (Medicaid) and 74.09.010(11) (CHIP). Therefore, only payments authorized by Washington’s Medicaid and CHIP programs are exempt.

Medicaid is [authorized] under RCW 74.09.510, which provides, “Medical assistance may be provided in accordance with eligibility requirements established by the authority, as defined in the social security Title XIX state plan for mandatory categorically needy persons . . . .” “Authority” means the Washington state health care authority. RCW 74.09.010(1).<sup>4</sup> We find no authority in chapter 74.09 RCW for payments under [out of state] Medicaid or CHIP programs. We conclude that the taxpayers could not deduct [out of state] Medicaid payments under RCW 82.04.4311(2).<sup>5</sup>

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<sup>4</sup> The CHIP program is defined in RCW 74.09.010(2).

<sup>5</sup> The taxpayers also contend that Medicaid payments, covered by Title XIX of the federal Social Security Act, are included in the second phrase, thereby qualifying [out of state] Medicare payments under the exemption. Yet, while the first phrase of the RCW 82.04.4311 expressly states “Title XVIII of the federal social security act,” the second phrase did not include the Title XIX language that the taxpayers argue should apply. Rather, the legislature used other language, referring to chapter 74.09 RCW, Washington law, not federal law. Where the legislature uses certain statutory language in one instance, and different language in another, there is a difference of legislative intent. *United Parcel Service, Inc. v. Dep’t of Revenue*, 102 Wn.2d 355, 362, 687 P.2d 186 (1984); *Agrilink Foods, Inc. v. Dep’t of Revenue*, 153 Wn.2d 392, 397, 103 P.3d 1226 (2005). Therefore, in the second phrase, the legislature intended to limit the deduction to programs under chapter 74.09 RCW.

The taxpayer also seeks a deduction from its gross income measure of B&O tax under RCW 82.04.4297, which provides:

In computing tax there may be deducted from the measure of tax amounts received from the United States or any instrumentality thereof or from the state of Washington or any municipal corporation or political subdivision thereof as compensation for, or to support, health or social welfare services rendered by a health or social welfare organization, as defined in RCW 82.04.431, or by a municipal corporation or political subdivision, except deductions are not allowed under this section for amounts that are received under an employee benefit plan.

To qualify for the RCW 82.04.4297 deduction, the receipts must be from “the United States or any instrumentality thereof or from the state of Washington or any municipal corporation or political subdivision thereof.” [The state] pays the taxpayers for medical services covered by . . . Medicaid. Those receipts are not from the United States, its instrumentalities, Washington or its political subdivisions. Therefore, we conclude that the taxpayers do not qualify for the RCW 82.04.4297 deduction.

Finally, the taxpayers seek to exclude payments from their medical benefit plan for medical services that they provide to their employees as interdepartmental charges. . . . Rule 201 defines “[interdepartmental] charges” as “amounts credited to the sales account or other gross income account of a taxpayer for goods, materials or services furnished by one department or branch of a business organization to another department or branch of the same business concern or firm.” The taxpayers provide medical services to their employees, not to other departments of the taxpayers. As part of its compensation for its employees, the taxpayers pay into the plan. The taxpayers’ payments into the plan are labor costs, and the plan’s payments to the taxpayers are for medical services provided to the employees. Those services are not provided for the taxpayers, but by the taxpayers for their employees.

Under the broad definition of gross income in RCW 82.04.080, a service provider may not deduct from its gross income any of its own costs of doing business, including its labor costs. *Rho Co. v. Dep’t of Revenue*, 113 Wn.2d 561, 582-583, 782 P.2d 986 (1989); *Pilcher v. Dep’t of Revenue*, 112 Wn. App. 428, 436, 49 P.3d 947 (2002). If the funds advanced by the self-insured medical plan were the taxpayers’ gross income, the taxpayers could not deduct their income from medical services for their employees.

The taxpayers also maintain that their recording of the value of their work done for their employees was not taxable under the Court’s ruling in *Weyerhaeuser v. Dep’t of Revenue*, 106 Wn.2d 557, 723 P.2d 1141 (1986) because the transfers were merely a management and reporting tool. According to the taxpayers the transfers served no substantive purpose. Unlike *Weyerhaeuser*, the taxpayers provided real medical services for their employees. The services were not “imputed” as was the interest in *Weyerhaeuser*. The money transferred for those services was gross income to the taxpayers under RCW 82.04.080.

We previously considered this issue in Det. No. 13-0198R, 33 WTD 204 (2014) where we concluded that a hospital owed B&O tax on amounts it receives from its self-insured medical insurance plan for medical services it rendered to its employees. 33 WTD at 211. We conclude that the Audit Division properly denied the taxpayers' refund request for B&O tax paid on medical services provided to its employees.

#### DECISION AND DISPOSITION

We deny the refund petitions.

Dated this 31<sup>st</sup> day of October, 2014.