F I S C A L I M P A C T R E P O R T

SPONSOR Sandoval **ORIGINAL DATE** 2/13/07 **LAST UPDATED** 3/15/07 **HB** 638/aHBIC/aSFC

SHORT TITLE Health Care Provider Gross Receipts **SB**

ANALYST Schardin/Francis

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY07	**FY08**		
	($72.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY07	**FY08**	**FY09**		
	($19,871)	($29,390)	Recurring	General Fund
	($3,388)	($4,160)	Recurring	Local Governments

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From: Several agencies responded to the underlying bills that are related to the provisions amended here.

SUMMARY

Synopsis of SFC Amendment

Hearing and Vision Aid Dispenser Gross Receipts: The amendment creates a new gross receipts tax deduction for receipts from the sale of vision and hearing aids or from fitting and dispensing of these types of aids.

Vision aids are defined as closed circuit television systems, monoculars, magnification systems, speech output devices or other systems specifically designed for use by persons with low vision or visual impairment and not normally used by a person who does not have low vision or visual

impairment. Visual impairment is defined as a central visual acuity of 20/200 or less in the better eye with use of a correcting lens, or a limitation in the fields of vision so the widest diameter of visual field subtends an angle of 20 degrees or less.

Hearing aids are defined as small electronic prescription devices that amplify sound and are usually worn in or behind the ear of a person with impaired hearing. Hearing aids include cochlear implants, amplification systems or other devices specifically designed for use by a person with hearing loss and not normally used by a person who does not have hearing loss. The effective date of these provisions will be July 1, 2007.

Hospital Gross Receipts Credit: The amendment creates a gross receipts tax credit for hospitals licensed by the Department of Health (for-profit hospitals). The credit equals roughly 20 percent of the state gross receipts tax rate in FY08, 40 percent in FY09, 60 percent in FY10, 80 percent in FY11, and the entire state gross receipts tax rate in FY12 and beyond. The provision will be applicable to tax reporting periods after July 1, 2007.

Indian Health Service Payment Gross Receipts: The amendment will allow receipts from payments by or on behalf of the Indian Health Service (IHS) of the United States Department of Health and Human Services for the provision of medical and other health services by medical doctors and osteopathic physicians to be deducted from gross receipts. The effective date of these provisions will be July 1, 2007.

Unpaid Health Services Gross Receipts Credit: The amendment creates a phased-in gross receipts tax credit that may be claimed by a medical doctor or licensed osteopathic physician for the value of unpaid medical care services provided while on call to a hospital. In FY08, a taxpayer's credit amount will equal 33 percent of the value of those unpaid services. In FY09, the credit will be equal to 67 percent of that value, and in FY10 and beyond, the credit will be for the full value.

The value of qualified services will be the amount charged for the services and may not exceed 130 percent of the reimbursement rate for the services under the Medicaid program. To qualify for the credit, medical services must remain unpaid after one year from the date of billing and must meet the following criteria: the services must have been provided to a person without health insurance or whose health insurance would not cover the services, who was not eligible for Medicaid. The services must also not be reimbursable under a program established in the Indigent Hospital and County Health Care Act (Chapter 27, Article 5 NMSA 1978). The effective date of these provisions is July 1, 2007.

Rural Health Care Practitioner Tax Credit: The amendment provides a personal income tax credit to health care practitioners who provide services in rural underserved areas. The credit may be carried forward for three years if the credit exceeds tax liability. The maximum allowable credit for physicians, dentists, osteopathic physicians, clinical psychologists, podiatrists and optometrists is $5 thousand. The maximum allowable credit for dental hygienists, physician assistants, certified nurse-midwives, certified registered nurse anesthetists, certified nurse practitioners or clinical nurse specialists is $3 thousand.

To qualify for the full credit, a practitioner must have provided health care for 2,080 hours at a practice site in an approved area. If the practitioner provided health care for at least 1,040 hours, the practitioner is eligible for 50 percent of the credit.

The Department of Health will determine whether the practitioner's application qualifies for the credit and will issue a certificate to the Taxation and Revenue Department. The credit is effective for tax years beginning with 2007.

Oxygen Delivery Gross Receipts: The amendment expands the gross receipts tax deduction for prescription drugs created in Section 7-9-73.2 to include oxygen and oxygen services provided by a licensed Medicare durable medical equipment provider. The effective date of this provision will be July 1, 2007.

Tax Incentives for Certain Health Insurers: The provision amends sections of the Insurance Code to provide an increased premium tax credit for health insurers who pay assessments to the New Mexico Medical Insurance Pool (NMMIP). Currently, health insurers who pay these assessments get a credit equal to 30% - 50% of the amount paid. The provision increases those credits to 50% of the assessed amount for most members and 75% of the assessed amount attributable to Pool policy holders that receive premiums through the federal Ryan White CARE Act, the Ted R. Montoya hemophilia program at the University of New Mexico health sciences center, the Children's Medical Services bureau of the Public Health Division of the Department of Health or other programs receive state funding or assistance. The effective date of these provisions is July 1, 2007.

Synopsis of Original Bill

Health Practitioner Deduction: House Bill 638 expands a gross receipts tax deduction for the receipts of certain health care practitioners from third-party administrators of Medicare and the federal TRICARE program to include receipts of doctors of social workers, oriental medicine, athletic trainers, chiropractic physicians, counselor and therapist practitioners, dentists, massage therapists, naprapaths, nurses, nutritionists, dieticians, occupational therapists, optometrists, pharmacists, physical therapists, psychologists, radiologic technologists, respiratory care practitioners, audiologists, and speech-language pathologists. The bill also provides definitions of these fields of health care.

Clinical Laboratories: House Bill 638 also amends expands the list of health practitioners who receive a gross receipts tax deduction for receipts from managed care providers, commercial health insurers and Medicare part C to include accredited clinical laboratories that are not located in a physician's office or hospital. Clinical laboratories were not included in 2004 legislation that made many other health provider receipts deductible from gross receipts tax. The effective date of the provisions in this bill is July 1, 2007.

FISCAL IMPLICATIONS

Appropriation Impacts of House Bill 638/aHBIC/aSFC

Title	FY08	FY09	FY10		
Indian Health Service Payment Gross Receipts	(72)	(76)	(79)	Recurring	General Fund
Sub Total - Amendments	(72)	(76)	(79)	Recurring	General Fund

Revenue Impacts of House Bill 638/aHBIC/aSFC

Title	FY08	FY09	FY10		
Hearing and Vision Aid Dispenser Gross Receipts	(740)	(780)	(815)	Recurring	General Fund
	(490)	(515)	(540)	Recurring	Local Governments
Hospital Gross Receipts Credit	(3,040)	(6,640)	(10,950)	Recurring	General Fund
Indian Health Service Payment Gross Receipts	(188)	(197)	(207)	Recurring	General Fund
	(125)	(131)	(138)	Recurring	Local Governments
Unpaid Health Services Gross Receipts Credit	(800)	(1,770)	(1,894)	Recurring	General Fund
	(550)	(1,180)	(1,263)	Recurring	Local Governments
Rural Health Care Practitioner Tax Credit	(3,400)	(3,400)	(3,400)	Recurring	General Fund
Oxygen Delivery Gross Receipts	(8)	(8)	(9)	Recurring	General Fund
	(5)	(6)	(6)	Recurring	Local Governments
Tax Incentives for Certain Health Insurers	(7,700)	(12,400)	(13,640)	Recurring	General Fund
Sub Total - Amendments	(15,876)	(25,196)	(30,915)	Recurring	General Fund
	(1,170)	(1,831)	(1,947)	Recurring	Local Governments
Health Care Provider Gross Receipts	(3,995)	(4,195)	(4,404)	Recurring	General Fund
	(2,218)	(2,329)	(2,445)	Recurring	Local Governments
Grand Total	**(19,871)**	**(29,390)**	**(35,319)**	**Recurring**	**General Fund**
	(3,388)	**(4,160)**	**(4,392)**	**Recurring**	**Local Government**

Hearing and Vision Aid Dispenser Gross Receipts: According to TRD, the 2002 Economic Census of Health Care Industries in New Mexico reports that offices of audiologists had total revenue of $9.2 million and offices of optometrists had revenue of $55.6 million in 2002. The estimated fiscal impact assumes that 75 percent of audiologist receipts and 10 percent of optometrist receipts would be eligible for the proposed deduction. After adjusting for inflation, that means about $18.7 million of receipts will be eligible for the deduction in FY08. Assuming a statewide tax rate of 6.6 percent, revenues will decrease by about $1,230 thousand. About 60 percent of this revenue loss will accrue to the general fund and about 40 percent will accrue to local governments.

Hospital Gross Receipts Credit: All of the state's for-profit hospitals are currently located within municipal areas, where the state tax rate is 3.775 percent. Therefore, the credit will eliminate the state gross receipts tax paid by for-profit hospitals once it is fully phased in. The bill does not apply to local option gross receipts taxes, so for-profit hospitals will still pay a little over 1 percent local gross receipts tax.

A New Mexico Hospital Association survey on hospital gross receipts indicates that for-profit hospitals paid gross receipts tax of $16.5 million in FY05 and $21.4 million in FY06, of which

60 percent went to the state and 40 percent went to local governments. Assuming that the impacted tax base will grow by 10 percent each year, the credit will reduce general fund revenue by about $3,040 thousand in FY08, $6,640 thousand in FY09, and $10,950 thousand in FY10, $16,062 thousand in FY11, and $22,086 thousand once it is fully phased-in in FY12.

Indian Health Service Payment Gross Receipts: TRD reports that a 2004 Legislative Council Service study showed total IHS spending in New Mexico for FY02 was $228.3 million. Adjusted for growth in the national IHS budget, TRD estimates total IHS spending in New Mexico to be $270 million in FY08. Federal survey data suggest that 22 percent of all health care spending is for physician services, suggesting payments of $60 million per year for IHS physician services. Some of these receipts are already eligible for gross receipts tax deductions under Sections 7-9-93 and 7-9-77.1 NMSA. After subtracting receipts eligible for these other deductions, TRD estimates a remaining tax base of $4.7 million in FY08. Based on a statewide tax rate of 6.6 percent, the bill will reduce revenue by about $313 thousand. Sixty percent of that revenue loss will accrue to the general fund and 40 percent will accrue to local governments.

Because the gross receipts tax deduction created reduces billing by providers to the Medicaid program the state will see budget savings in the Medicaid program. New Mexico's average share of Medicaid spending is 23 percent, so Medicaid savings are expected to be 23 percent of the $313 revenue impact explained above, or $72 thousand.

Unpaid Health Services Gross Receipts Credit: A study by the Legislative Health and Human Services Committee entitled, "House Bill 955: Comprehensive Study on Health Care and Health Care Costs in New Mexico," stated that in 2002, the New Mexico Hospital Association reported total uncompensated care of $209 million. Growing that figure by 7 percent per year, the rate of medical inflation, yields an estimate of $313.7 million total uncompensated care in FY08. The New Mexico Medical Society reports that only 300 physicians would likely be eligible for the proposed gross receipts tax credit based on the assumption that only surgeons are normally on call.

TRD estimates that the credit will be equal to about $35 thousand per physician, for a total credit amount of $10.5 million. However, TRD believes that tax liability for these 300 physicians will only be about $13.2 thousand, or a total of $3,630 thousand. TRD assumes the credit will be nonrefundable, so the fiscal impact will be capped at $3,630 thousand. The fiscal impact of the bill is expected to phase in over a few years because services must remain unpaid for one year to receive the proposed credit. About 60 percent of each year's fiscal impact is expected to impact the general fund, while the remaining 40 percent will impact local governments. The fiscal impact is expected to grow by about 7 percent per year.

Rural Health Care Practitioner Tax Credit: Based on information from the Department of Health, TRD estimates that about 900 practitioners will be eligible for the $5 thousand credit. Multiplying this population by the maximum credit amounts yields a potential revenue loss of $5.5 million. This impact was then adjusted downward to 40 percent of that amount to reflect the following considerations:

(1) A 2003 report by the N.M. Health Policy Commission estimated that approximately 55 percent of the respondents to a survey of licensed practitioners were actively practicing medicine in New Mexico. Many were practicing in other states or retired. A separate study by the Center for Health Workforce Studies estimated that only 52 percent of licensed physicians were actively practicing in the state.

(2) Some of the practicing physicians living in rural areas may be practicing only pat-time in the rural area, thus they will receive the reduced tax credit.

(3) A $3,000 tax credit could offset tax on about $60,000 of taxable income, equivalent to about $75,000 of total income. A $5,000 credit could completely offset tax on $100,000 of taxable and $125,000 of total income. Many but not all practitioners will be able to exhaust the full credit amount.

Oxygen Delivery Gross Receipts: Under current law, TRD is already counting oxygen as a prescription drug, so the bill would only extend the deduction to oxygen and oxygen services that are not prescribed by a doctor. TRD believes this will impact a small number of transactions with tax base of about $200 thousand per year. Taxed at a statewide rate of 6.6 percent, the proposal would reduce revenue by about $13.2 thousand per year. About 60 percent of that revenue loss would be to the general fund and the remaining 40 percent to local governments.

Tax Incentives for Certain Health Insurers: Insurance premium taxes are collected by the Public Regulation Commission for the benefit of the general fund. Thus, premium tax credits reduce the amount of premium tax revenue to the general fund. NMMIP has projected future assessments to grow from more than $20 million in 2006 to $50 million in 2009.

Under current law, the 30 and 50 percent tax credits result in a $14.6 million revenue loss for the general fund for FY08. Under projections provided by NMMIP, the 50 and 75 percent tax credits proposed in this bill result in a $22.3 million general fund revenue loss – a $7.7 million difference.

Under current law, and assuming the same rate of growth in the 2008 assessment, the revenue impact of the 30 and 50 percent credits for FY09 is $32.5 million. The 50 and 75 percent tax credits proposed in this bill result in a $44.9 million general fund revenue loss – a $12.4 million difference. The projections assume the same in growth rate in the tax credit for the 2008 assessment as in the 2007 assessment. This near doubling rate of growth is not expected in future years as the Pool reaches its saturation point.

Health Practitioner Deduction: TRD reports that according to the Centers on Medicaid and Medicare (CMS), total Medicare spending in New Mexico was $1.3 billion in 2004, a figure that is expected to grow by about 10 percent per year. Currently, gross receipts tax deductions are provided for receipts from Medicare for certain physicians' services, nursing homes, clinical laboratories, and home health care services. The remaining taxable gross receipts of physicians addressed in the amendments to Section 7-9-77.1 are estimated to be $82.5 million in FY08. Taxed at a statewide average rate of 6.6 percent, these amendments will reduce revenue by about $5,545 thousand. About 60 percent of this revenue loss will accrue to the general fund, while 40 percent will be to local governments.

Clinical Laboratories: Based on the Report 80, TRD believes taxable gross receipts for clinical labs not located in a physician's office or a hospital will be $54 million in FY08. Based on information from the federal Centers for Medicaid and Medicare Services (CMS) and from industry representatives, about 75 percent of that total comes from facilities not associated with physicians' offices or hospitals, and about 25 percent of these receipts come from managed care insurers. Therefore, the fiscal impact to the general fund from the amendments to Section 7-9-93 NMSA 1978 is estimated to be $668.3 thousand in FY08 ($54 million X 75 percent X 25 percent eligible receipts X 6.6 percent statewide tax rate). This impact includes the direct impact of

making these clinical laboratory receipts deductible, as well as the impact of holding local governments harmless from the new deductions.

SIGNIFICANT ISSUES

Hearing and Vision Aid Dispenser Gross Receipts: According to the National Center on Hearing Assessment and Management, one in 10 Americans has hearing loss. However, about 30 percent of those (2.8 million) do not have hearing aids because they are unaffordable. DOH reports that in 2006, the average cost of one hearing aid, accessories and related professional services is about $3 thousand. The cost to an individual requiring two hearing aids would be about $6 thousand.

Hearing loss is one of the most common birth defects in the United States. According to DOH, about 80 infants with significant hearing loss are born in New Mexico each year. Hearing loss prevalence increases with age: about 31 percent of New Mexicans over the age of 65 experience hearing loss and DOH estimates that 70 to 90 percent of New Mexicans in nursing homes experience hearing loss.

DOH reports that over half of New Mexicans under the age of 21 are enrolled in Medicaid, which covers hearing and vision aids. Still, access to appropriate hearing and vision aids and related services is limited due to Medicaid's low reimbursement rate and coverage limits. The New Mexico Medical Insurance Pool covers hearing aids but requires high deductibles. Hearing aids are not covered under Medicare and a DOH survey of New Mexico's largest HMO/PPO plans found that hearing aids are excluded from coverage.

For children, vision aids may be covered by the Public Education Department during the school year, but not for home use. Insurance rarely covers durable medical equipment such as the types of vision aids that will qualify for the deduction created in this bill. While working adults may be able to acquire vision aids through the Commission for the Blind and Visually Impaired, senior citizens who are not seeking employment will not be served by that commission.

Hospital Gross Receipts Credit: Under current law, for-profit hospitals qualify for a 50 gross receipts tax deduction (Section 7-9-73.1 NMSA 1978). The bill effectively reduces the gross receipts tax paid by for-profit hospitals from 50 percent of the normal state rate to nothing once it is fully phased-in in FY12.

About half of New Mexico's hospitals are for-profit. For-profit hospitals compete with non-profit hospitals in New Mexico and hospitals in neighboring states that do not pay gross receipts tax. The New Mexico Hospital Association reports that this bill will remove a competitive disadvantage against New Mexico's for-profit hospitals.

According to the NMHA, rural hospitals have no choice but to absorb the costs of uncompensated care for patients who cannot pay. In addition, it is difficult for for-profit hospitals to pass gross receipts tax on to consumers because Medicare will not reimburse for it.

Indian Health Service Payment Gross Receipts: According to DOH and IAD, the proposed gross receipts tax deduction would make it more profitable for medical providers to serve Native American populations in New Mexico. Currently, 31 of New Mexico's 33 counties are designated as health professional shortage areas for primary care physicians.

IAD reports that Indian Health Service and tribal health care programs currently face difficulties in recruiting health care practitioners due to below-average salaries.

Unpaid Health Services Gross Receipts Credit: According to DOH, the New Mexico Medical Society identified reducing gross receipts taxation on health services and reducing the burden of uncompensated care for indigent patients as areas of concern for health practitioners in New Mexico. This provision addresses these concerns by allowing physicians to reduce gross receipts tax liability in proportion to the amount of uncompensated care they provide.

According to DOH, about 21 percent of New Mexicans are uninsured. In 2002, the National Center for Health Workforce Analysis documented that 32.5 percent of New Mexicans live in areas with a shortage of primary health care professionals. Currently, 31 of New Mexico's 33 counties are designated as health professional shortage areas for primary care physicians.

Rural Health Care Practitioner Tax Credit: According to DOH, this provision would establish a major new financial incentive for the recruitment and retention of health care practitioners in rural underserved areas. In preliminary planning conducted by TRD and DOH, it was estimated that as many as 750 individuals might participate, with tax credits totaling as much as $3.5 million per year.

Several states have similar programs. Oregon has had a statewide program of this type in place for over a decade, with more than 1,500 participants each year. Program officials in Oregon report that their tax credit is an effective way to provide incentives to needed health care practitioners, particularly in the area of retention. The credit would be more comprehensive than Oregon's.

Oxygen Delivery Gross Receipts: Oxygen used for breathing and prescribed and administered by a physician already qualifies as a prescription drug under section 201(g)(1) of the federal Food, Drug, and Cosmetic Act [21 USC 321(g)(1)] because it is intended for use in the cure, mitigation, treatment, or prevention of disease.

Tax Incentives for Certain Health Insurers: The Medical Insurance Pool, established by Chapter 54 of the Insurance Code, is a non-profit entity operating a high-risk health insurance pool. The premiums charged to members are not sufficient to cover the costs, and this shortfall is assessed to the health insurance industry. Assessed insurers then receive a 30 percent premium tax credit for full premium plan losses and a 50 percent premium tax credit for reduced premium plan losses.

The pool projects increases in the assessments levied on the health insurance industry. The growth in these assessments is primarily the result of increased membership in the pool and expansion of the reduced premium plan, which is available to low income persons. The projected growth is also from the executive's Insure New Mexico initiatives. Since the growth in assessments is primarily coming from the low-income subsidy and Insure New Mexico, this provision proposes shifts the cost from the commercial insurance industry to the state government.

Health Practitioner Deduction: Recruitment and retention of health providers has been difficult in New Mexico because of the gross receipts tax. Economic theory suggests that a shortage of

healthcare labor will push healthcare wages, and therefore healthcare costs higher. Although much of this problem was addressed in 2004 when Section 7-9-93 NMSA 1978 was enacted, some healthcare practitioners in New Mexico still pay gross receipts tax, while their counterparts in most other states do not. Unlike many businesses that are subject to gross receipts tax but pass the tax on to consumers, many health providers cannot pass the tax on because managed care organizations and Medicare refuse to pay the tax.

According to the Health Policy Commission, in 2006, New Mexico ranked 4th lowest in the nation in dentists per capita, 6th lowest in pharmacists per capita, 8th lowest in registered nurses per capita, and 11th lowest in optometrists per capita. However, New Mexico ranked in the top twelve states in terms of physical therapists, psychologists, speech and language pathologists, and occupational therapists per capita. This suggests the provision could be more effective if it amended Section 7-9-77.1 NMSA 1978 by adding only the types of practitioners in short supply in New Mexico.

TRICARE is a managed care health insurance program for active duty military, active duty service families, military retirees and their families, survivors, and active duty Reservists and National Guard.

ADMINISTRATIVE IMPLICATIONS

Unpaid Health Services Gross Receipts Credit: TRD reports that up to 3 FTE will be required to process the credit because thousands of claims will have to be processed manually. Instructions and publications will require revision and taxpayers and employees will require education.

Determining the allowable credit will require a high level of audit and compliance efforts. TRD auditors will need to determine maximum reimbursement rates, whether a doctor was on-call, whether services were performed in a hospital rather than a physician's office, whether the service recipient was eligible for Medicaid, and whether one year has passed since billing.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Hearing and Vision Aid Dispenser Gross Receipts: Relates to HB 389 and HB 89.
Hospital Gross Receipts Credit: Relates to HB 524, SB 326, HB 23, and SB 161.
Indian Health Service Payment Gross Receipts: Relates to HB 245 and SB 11.
Unpaid Health Services Gross Receipts Credit: Relates to HB 958 and SB 187.
Tax Incentives for Certain Health Insurers: Relates to SB 565 and HB 1164.
Health Care Provider Gross Receipts: Relates to SB 684, HB 797 and SB 893.

TECHNICAL ISSUES

Indian Health Service Payment Gross Receipts: IAD recommends adding a definition of the term "covered beneficiaries." A suggested definition may be found in the federal Indian Health Care Improvement Act, Public Law 94-437, which defines the term "Indian."

Unpaid Health Services Gross Receipts Credit: The provision does not clarify whether or not the gross receipts tax credit created is refundable or not. TRD reports that in the absence of refundability language it will be presumed to be nonrefundable. If this presumption is

successfully challenged, credit claims could be as large as the entire gross receipts tax base for the credit, which was estimated to be $47 million.

The provision does not clearly define the terms "on-call" or "hospital."

DOH recommends clarifying the definition of "qualified health care services" to limit the credit to uncompensated care provided in hospital clinics and emergency rooms by physicians with staff privileges.

TRD suggests adding a recapture provision in the event that a physician receives payment for services after claiming the credit.

TRD notes that Section 7-9-67 NMSA 1978 allows taxpayers reporting on an accrual accounting basis to claim a deduction for uncollectible receipts. The bill would allow physicians that report on an accrual basis to request a deduction and claim the credit, while cash basis physicians would only be eligible for the credit.

Health Care Provider Gross Receipts: TRD notes that Section 7-9-93 might not be the right location for the clinical laboratory deduction proposed in this bill because it adds clinical laboratories to the list of health *practitioners.* However, clinical laboratories are defined as health *facilities* under 42 U.S.C. Section 263a.

Clinical Laboratories: The Health Policy Commission notes that receipts of a clinical laboratory in a free-standing clinic or anatomical laboratory owned by a pathologist will not receive the clinical laboratories gross receipts tax deduction created in the bill. If this is not the intent of the bill, HPC recommends deleting the words, "in a physician's office or."

SS/mt