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

SPONSOR Papen **ORIGINAL DATE** 01/30/12 **LAST UPDATED** 02/10/12 **HB**

SHORT TITLE Medical Equipment & Supply Gross Receipts **SB** 188/aSCORC

ANALYST Walker-Moran

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY12	FY13	FY14	FY15	FY16		
$0.0	($700 - $5,800.0)	($800 - $6,500.0)	($900 - $7,200.0)	($1,000 - $8,100.0)	Recurring	Local Governments
$0.0	($900 - $6,900.0)	($1,000 - $7,700.0)	($1,100 - $8,600.0)	($1,200 - $9,600.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates HB 192 (if amended)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Aging and Long-Term Services Department (ALTSD)
Human Services Department (HSD)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of SCORC Amendment

The Senate Corporations and Transportation Committee amendment changes language in the deduction to read "if provided by a licensed durable medical equipment provider certified by medicare and medicaid," rather than the previous language which said, "a licensed medicare durable equipment provider." It also removes the language regarding a licensed medicare durable medical equipment provider from the part of the deduction that mentions oxygen and oxygen services. The amendment also adds a new subsection requiring that the deduction shall only be taken by a taxpayer whose gross receipts are no less than ninety percent derived from the sale of prescribed medical equipment or supplies.

Synopsis of Original Bill

Senate Bill 188 amends Section 7-9-73.2 NMSA 1978 to expand the gross receipts tax and

governmental gross receipts tax deduction for prescription drugs and oxygen to include durable medical equipment (DME) and medical supplies.

The purpose of the deduction is to help retain businesses in New Mexico that sell DME, including oxygen and oxygen services and medical supplies and to provide prescription drugs to New Mexicans without the added cost of taxation.

The effective date of this bill is July 1, 2012. There is no sunset date. The LFC recommends adding a sunset date.

FISCAL IMPLICATIONS

This bill may violate the LFC tax policy principle of adequacy. According to the LFC General Fund Recurring Appropriation Outlook for FY14 and FY15 the December 2011 forecasted revenues will be insufficient to cover growing recurring appropriations. Since currently forecasted revenues in FY14 and FY15 may not be adequate to fund government services there is insufficient funds for additional tax cuts. It also violates the LFC tax policy principle of efficiency by narrowing the tax base.

Per TRD: According to the Centers for Medicare & Medicaid Services report, Total Medicare personal health care spending by state and by service (1991-2009)[1], New Mexico Medicare expenditures in 2009 on durable medical products were about $65 million with 5% four-year average annual growth rate; prescription drugs and other non-durable medical product was about $323 million with 19% four-year average annual growth rate. Non-durable medical product is estimated approximately 17% of the total prescription drugs and other non-durable medical product expenditures. This calculation shows the upper bound on the fiscal impact.

The SCORC amendment excludes pharmacies and large multistate medical equipment sellers from the deduction. According to the information provided by the industry, there are about 54 New Mexico durable medical equipment suppliers licensed by Medicare and Medicaid, and whose sales are no less than 90% prescribed durable medical equipment or prescribed medical supplies. The industry estimates that the fiscal impact would be 1/8 of the upper bound with the amendment. The reason both the upper and lower bounds are reported is that the TRD feels that it would be unable to administer the relatively subtle distinction proposed by the amendment.

There is no fiscal cost to HSD. When Medicaid pays providers for these items, gross receipts tax is not applicable because they are tangible items (as opposed to services) which are not taxable to the state as a purchaser. There is no fiscal cost to ALTSD.

SIGNIFICANT ISSUES

According to HSD, even as amended, SB188 has a number of issues with its clarity, application, and intent:

The amendment attempts to make it clear that the oxygen supplier and durable medical equipment provider must participate in Medicare and Medicaid by stating they must be "certified by Medicare and Medicaid." However, neither Medicare nor Medicaid actually "certify" these

[1] Please see http://www.cms.gov/NationalHealthExpendData/downloads/resident-state-estimates.zip.

providers, as that term is typically used by Medicare and Medicaid to designate a specific inspection requirement for providers. Rather these providers simply "participate" in Medicare and Medicaid.

The amendment specification that the deductions provided for durable medical equipment and medical supplies can only be taken by taxpayers whose gross receipts are no less than 90% derived from the sale of durable medical equipment and supplies helps identify the applicable providers but likely would create confusion for a provider who may also dispense drugs and/or supply oxygen in addition to supplying durable medical equipment and medical supplies because it would be difficult for such a provider to achieve the 90% requirement for the medical equipment and medical supply line of business alone. This will require reporting by businesses and additional monitoring by the New Mexico Taxation and Revenue Department.

Also, because only the sale of equipment is included, and apparently not the rental, it is unlikely any provider could achieve the 90% requirement for the medical equipment and medical supplies unless the rental of equipment is also included in the bill.

The bill only allows for the tax deduction for the "sale" of these items. Most durable medical equipment is rented for up to ten months under Medicare and Medicaid, at which time the rental payments have reached specified amounts, meaning that Medicare and Medicaid then consider it the property of the individual. However, the current interpretation of state tax law is that a rental is a "service," not the sale of a tangible item, and therefore is subject to gross receipts tax when the State is the buyer. To ensure the law is clear, the wording should specifically state that rental of durable medical equipment is also allowed the intended deduction.

Oxygen gas and oxygen concentrators are not, in fact, sold at all under Medicare or Medicaid. Rather, there is an initial period of capitation rental payments after which time an ongoing monthly maintenance fee is allowed. To ensure the law is clear, the wording should specifically state that maintenance fees, repairs, and customizations are also allowed deductions for durable medical equipment and oxygen providers.

Also, a point of confusion is how deductibles, co-insurance, and copayments are handled in the tax law. Often for these items, the amount of the patient's financial responsibility for deductibles, co-insurance, and deductibles are substantial. A medical equipment supplier receives a significant amount of payment from Medicaid, other insurers, and from private paying patients; the bill is not clear if these payments are allowed as deductions by the taxpayer.

Currently, despite the stated intent of the bill "to provide prescription drugs to New Mexicans without the added cost of taxation", copayments for drug items under HMO rules are still often taxed. With some drugs being very costly, the copayment or a co-insurance of 20 percent (or sometimes higher) can be in the hundreds of dollars. Some insurance companies actually have co-payments or co-insurances of 100 percent for some drug items, which is better for a patient than if the insurer did not cover the drug at all because then the patient's responsibility is limited to 100 percent of what the insurance company would have paid, not the usual charge of the drug. Some pharmacies currently charge patients gross receipts tax on these costly items in the form of applying gross receipts tax to co-insurance or copayments. The bill needs to be clear if co-payments, co-insurance, and deductible amounts paid to the medical supplier or pharmacy are also applicable for the deduction.

The requirement that items need to be prescribed is appropriate, as is the requirement for Medicare participation on the part of the provider to distinguish purchases from grocery stores, etc. However, it is not clear that payment for a medical supply item sold by a pharmacy is an allowed deduction. Typically, diabetic glucose monitoring kits, slings, bandages, etc., are sold by pharmacies, but they are not actually prescription drugs, even if prescribed by a practitioner and dispensed by a pharmacy. Under the definitions, it appears that a durable medical supplier can deduct these sales from gross receipts tax but a pharmacy cannot.

There have been a decreasing number of durable medical equipment providers in New Mexico participating in the Medicaid program. Durable medical equipment providers who participate in Medicare always participate in Medicaid, so Medicare participation is probably not very good either. This appears to result from a decreasing type of business of this nature in New Mexico, rather than because the providers are unwilling to participate in Medicare and Medicaid. It is not known if these tax changes will have an impact or not, as it seems that ultimately the patient, rather than the business, is who benefits.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met when TRD is required to report annually to the interim legislative revenue stabilization and tax policy (RSTP) committee aggregate amounts of each deduction taken, the numbers of taxpayers claiming the deduction and other information to determine whether the deduction is meeting its purpose.

According to TRD, requiring taxpayers to separately state deductions is an inaccurate method of capturing this information. Historically, the TRD has found that taxpayers do not follow this instruction very well, since there is no penalty or consequences of failure to report or failure to report correct information. In addition, confidentiality laws (Section 7-1-8 NMSA 1978 et. seq.) may limit the information that can be reported to the RSTP committee in determining if the deduction is performing its purpose.

ADMINISTRATIVE IMPLICATIONS

There is minimal impact on TRD. Regulations and systems would need modification and development. Extra taxpayer and department employee education would be needed.

OTHER SUBSTANTIVE ISSUES

According to TRD, this bill intends to cut out pharmacies and multistate sellers from durable medical equipment suppliers certified by Medicare and Medicaid. On its face, this looks like an extension of the medical services deduction at Section 7-9-93 NMSA 1978. This was enacted primarily because Medicare does not reimburse the providers for their gross receipts taxes paid. Thus, doctors and other health care providers working in the State were receiving less net compensation than their colleagues working in other states.

ALTERNATIVES

The HSD recommends that in place of “certified by Medicare and Medicaid”, replace the wording with “participating in Medicare and Medicaid.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

EWM/svb:amm