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SENATE COMMITTEE ON ECONOMIC DEVELOPMENT & TAXATION

TESTIMONY REGARDING HB 2306 HD 2 SD 1 RELATING TO GENERAL EXCISE TAX

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)

DATE: MARCH 18, 2008

TIME: 1:15PM

ROOM: 224

This legislation provides a general excise tax exemption for managed care support contractors of the TRICARE program that is established under 10 United States Code chapter 55.

The House Committee on Public Safety & Military Affairs amended the measure to clarify that the exemption applies to reimbursements.

The House Committee on Finance amended the measure's effective date.

The House of Representatives passed this measure on third reading.

The Senate Committee on Health amended the measure by making its effective date retroactive.

The Department of Taxation has **no comments** on this legislation other than citing that this was not factored into the Executive Budget or any of its fiscal priorities this session.

Because this measure was amended to provide retroactive tax relief for any contractors that participate in the TRICARE program, the Department is precluded from providing a specific estimate because of the limited taxpayer population of which the Department utilizes to arrive at its revenue estimates. The Department suggests that the Committee determine the revenue loss of any proposed retroactive tax relief by discussing the matter directly with taxpayers that will benefit from the measure.

HMSA



Blue Cross
Blue Shield
of Hawaii

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MAR 17 2008

March 18, 2008

The Honorable Carol Fukunaga, Chair
The Honorable Will Espero, Vice Chair

Senate Committee on Economic Development and Taxation

Re: HB 2306 HD2 SD1 – Relating to General Excise Taxation

Dear Chair Fukunaga, Vice Chair Espero and Members of the Committee:

The Hawaii Medical Service Association (HMSA) appreciates the opportunity to testify in support of HB 2306 HD2 SD1 which would exempt from the general excise tax amounts received by managed care support contractors as reimbursements of costs or advances made pursuant to a contract for the administration of the federal TriCare program.

This measure would clarify that any amounts received by a managed care support contractor for reimbursements of costs made by the contractor, made pursuant to the contract with the federal government for the administration of the TriCare program, are exempt from the Hawaii General Excise Tax. It seems, at this time, it is unclear as to whether or not TriCare reimbursements are indeed subject to the GET.

HB 2306 HD2 SD1 would clear up any confusion on this issue and bring Hawaii in line with every other state in the U.S. (except Texas), that has put this exemption into law. This exemption will truly support the continued availability and strength of the TriCare program and ensure that it is able to provide coverage to the approximately 150,000 current and former military personnel and their family members who reside in Hawaii.

Thank you for the opportunity to provide testimony on HB 2306 HD2 SD1.

Sincerely,

Jennifer Diesman
Assistant Vice President
Government Relations

TAXBILLSERVICE

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TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: GENERAL EXCISE, Exempt reimbursements for TRICARE program

BILL NUMBER: HB 2306, SD-1

INTRODUCED BY: Senate Committee on Health

BRIEF SUMMARY: Amends HRS section 237-24.75 to clarify that amounts received by a managed care support contractor of the TRICARE program established under the 10 United States Code chapter 55 for reimbursement of costs or advances made to health care providers pursuant to a contract with the United States shall be exempt from general excise taxation.

EFFECTIVE DATE: Retroactive to January 1, 2005

STAFF COMMENTS: The TRICARE program was established by the U.S. Department of Defense (DOD) as the managed care component of the Military Health Care system to augment the health care services provided to DOD personnel at military treatment facilities. TRICARE contracts with third-party administrators (managed care support contractors) to establish and maintain networks of TRICARE-authorized civilian health care providers. These managed care support contractors make advances to health care providers for the services they provide to TRICARE beneficiaries and are reimbursed by the DOD for the amounts of such advances.

This measure clarifies that amounts received by the managed care support contractors as reimbursements from the DOD for advances they made on behalf of the DOD for TRICARE program purposes are not taxable under Hawaii's general excise tax law.

While an understanding of HRS section 237-20 which delineates the cost reimbursement provision under the general excise tax law appears to dictate that such reimbursements are not taxable unless the person making the advance receives additional monetary consideration for the services provided, the adoption of this measure may be unnecessary.

On the other hand, if the third party administrator receives a fee for handling these reimbursements, then it runs into the ban that HRS 237-20 imposes where the fee taints the entire amount received from the DOD. Hawaii law has already set precedent, providing that amounts received as reimbursements for wages, salaries and benefits of hotel workers paid by a hotel operator on behalf of the hotel owner are exempt as are reimbursements made on behalf of the city for the operations of the city's bus system by a third party operator even though additional consideration is received in both cases. It should be noted that the fee paid to the third party administrator would continue to be subject to the general excise tax as the fee is gross income to the third party administrator.

Digested 3/17/08

GOODSILL ANDERSON QUINN & STIFEL

A LIMITED LIABILITY LAW PARTNERSHIP LLP

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March 18, 2008

TO: Senator Carol Fukunaga
Chair, Senate Committee on Economic Development & Taxation
Hawaii State Capitol, Room 216
Via Email: testimony@capitol.hawaii.gov

FROM: Chris Pablo

RE: **H.B. No. 2306 HD2 SD1– Relating to General Excise Tax
Hearing on Tuesday, March 18, 2008 at 1:15 pm, Room 224**

Dear Chair Fukunaga and Members of the Committee on Health:

I am Chris Pablo testifying on behalf of TriWest Healthcare Alliance Inc. (“TriWest”), a Delaware corporation headquartered in Phoenix, Arizona. **TriWest supports HB 2306 HD2 SD1.**

TriWest is one of several regional third-party administrators or fiscal intermediaries of a cost-effective, high quality network of health care providers for the nation's active and retired uniformed service members and their families, under a federal government program known as “TRICARE” and formerly known as “CHAMPUS.”

What is TRICARE? The Federal Government has established a managed health care program for members of the uniformed services and certain dependents. It was created in the early 1990s to supplement the existing military health care delivery system and provide health care services for active duty military personnel, military retirees, and their families (collectively, the “Beneficiaries”) by utilizing civilian health care providers.

In Hawaii, the Beneficiaries have access to the military health care facilities, such as the Tripler Army Medical Center and to health care clinics on military bases through the state. In addition, the Beneficiaries have access to medical services through the network of community health care providers that has been created by TriWest.

TRICARE receives its funding as part of the annual defense appropriations budget. It is administered by the TRICARE Management Activity (“TMA”), which is part of the United States Department of Defense (“DoD”), Office of the Assistant Secretary of Defense (Health Affairs).

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What is TriWest? In the health care industry, TriWest's business would be characterized as a "**third-party administrator**." TriWest, known as a "**managed care support contractor**" in the applicable Federal laws and regulations, is a disbursing agent for the Federal Government in the western states, including Hawaii. Its job is to receive claims and invoices from health care providers, and then pay those claims according to the amounts and guidelines set by the Government ("**reimbursement**"). The Government then reimburses TriWest for the amounts paid, and also pays TriWest an **administrative fee** for its services. This is best illustrated in the attached PowerPoint slide.

TriWest pays Hawaii General Excise Tax on the amounts it receives from TRICARE as compensation for its services as *managed care contractor*, but it does not pay tax on the reimbursement amounts. In prior discussion with representatives of the Department of Taxation, there was some concern that the reimbursement amounts might be taxable. If they are taxable, the costs for health care of uniformed service members would increase significantly. TriWest is asking the Department of Taxation for formal clarification of this issue, and is concurrently asking the Legislature for similar relief.

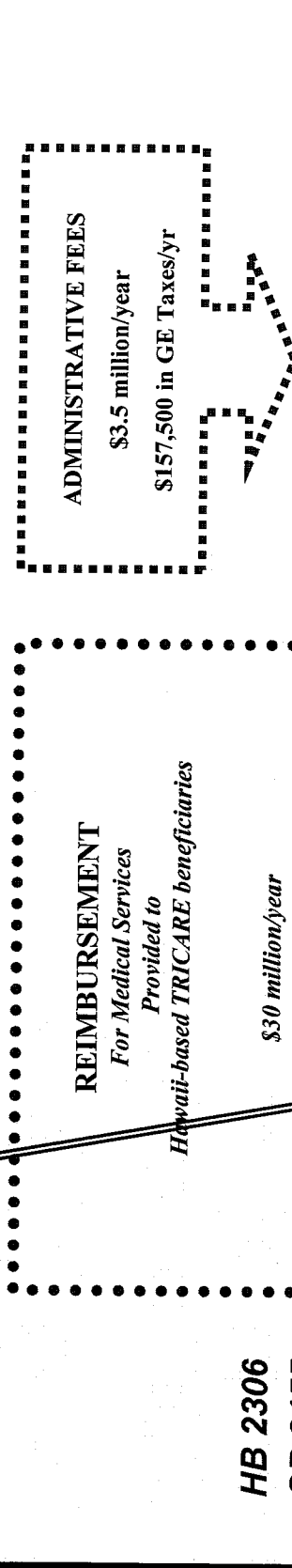
What is the purpose of HB 2306 HD2 SD1? The purpose of HB 2306 HD2 SD1 is to make clear that the amounts received by TriWest from TRICARE as "reimbursements" are exempt from the imposition of the General Excise Tax by amending Section 237-24.75 by adding a new subsection (3). The proposed subsection (3) will read, as follows:

"Amounts received by a managed care support contractor of the TRICARE program that is established under 10 United States Code chapter 55, *as amended*, for reimbursement of costs or advances made pursuant to a contract with the United States; and"

We thank you for the opportunity to testify in support of HB 2306 HD2 SD1.

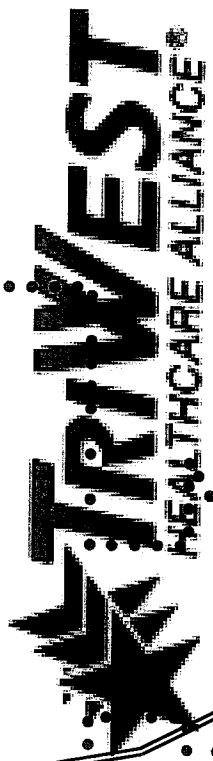


US Department of Defense
Military Health System



HB 2306
SB 2155

Propose to
Amend §237-24.75
to address the
"pass through"
of
reimbursements



aka "TPA"
Third-party Administrator

Managed care support contractor

Network Health Care Providers

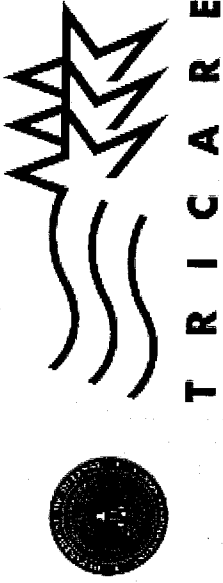
Medical services & supplies



Soldiers, Sailors, Airmen, Dependents, Retirees

Beneficiaries

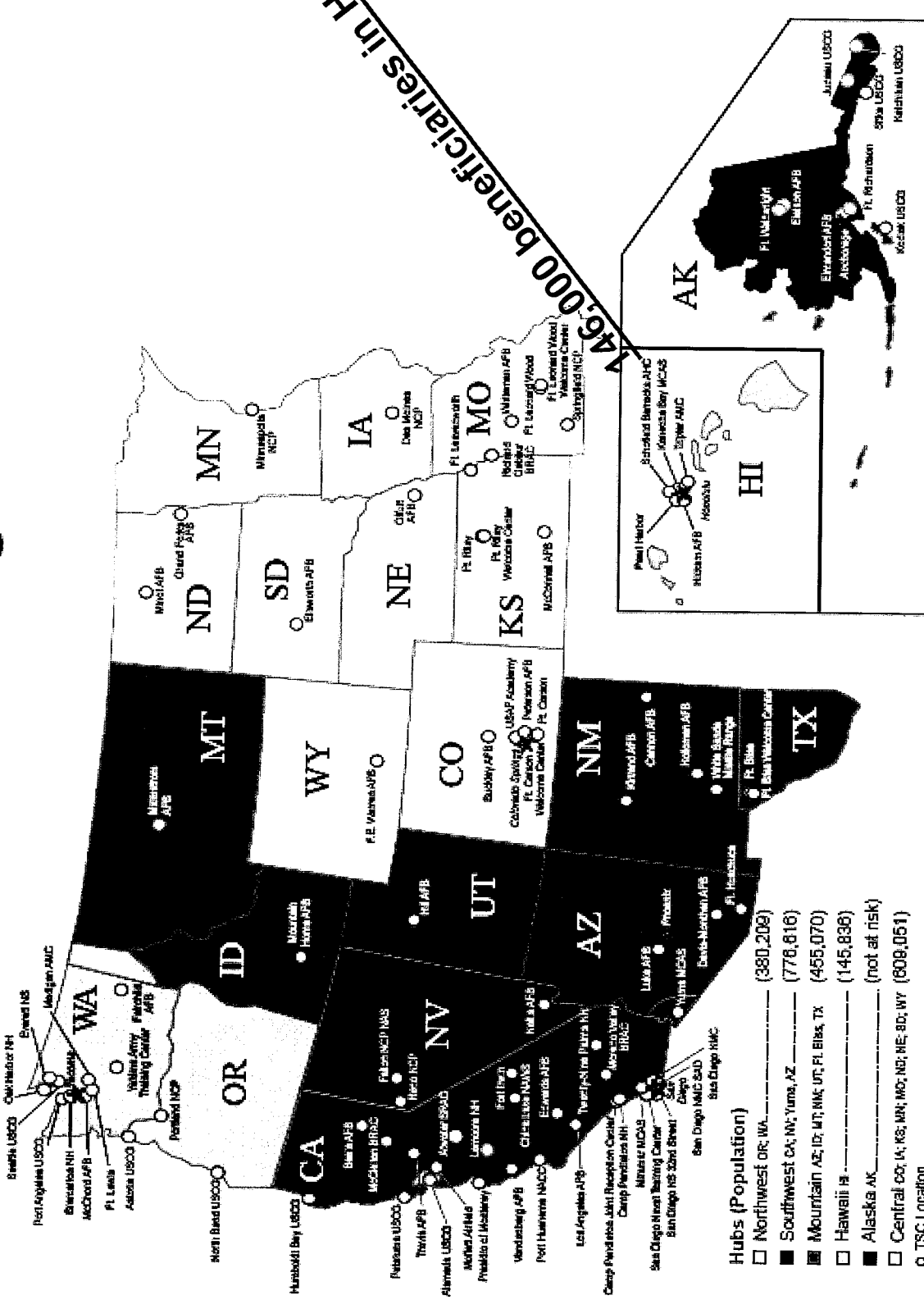
Who's who? What it is and What it's not



- Federal government program fka CHAMPUS nka TRICARE
- U.S. Dept. of Defense (DoD) health care entitlement program for "beneficiaries":
 - Active duty, guard and reserve
 - Military retirees
 - Dependents and survivors
- Optimizes delivery at military treatment facilities by supplementing access to civilian health care networks
- Funding from the DoD budget
- NOT an insurance plan, but rather a health care entitlement earned by military members for their service to our country

- Privately held, Phoenix-based corporation
- Contractor with DoD – *managed care support contractor* [10 USC Chapter 55]
- "Third-party administrator" (TPA) or "fiscal intermediary"
- Contracts with private-sector health care providers to serve "beneficiaries"
- Administers 21-state TRICARE West Region
 - Hawaii: serves 146,000 *beneficiaries*
- Monitored by TRICARE Management Authority, a department within DoD
- NOT an insurance company
- NOT a health care provider

TRICARE West Region Overview



46,000 beneficiaries in Hawaii!

The TRICARE West Region includes the 21 states identified above and a section of western Texas, including El Paso and the area surrounding Fort Bliss. Exceptions: The Rock Island Arsenal area of Iowa, and certain ZIP codes in St. Louis, MO.

Does TriWest pay general excise taxes?

- **Yes!**
- **\$157,500 per year in general excise tax** is paid to the State of Hawaii on gross receipts of \$3.5 million
- Taxable gross receipts of \$3.5 million per year are paid by TRICARE to TriWest for various Administrative fees:
 - Clinical Support Fee
 - Disease Management Program Fees
 - Enrollment Fees received from “beneficiaries”
 - Claims processing fees
 - Underwriting Fee
- **SB 2155 and HB 2306 do not affect nor change this!**

What's the purpose for SB 2155 and HB 2306?

- In prior discussions with representatives of the Department of Taxation—they expressed some concern that the ***reimbursements*** might be taxable
- Consequences if taxable:
 - Costs for health care of military ***beneficiaries*** would significantly increase
 - Can't pass on GET expense to TRICARE/DoD, i.e., the federal government

What will SB 3155 and HB 2306 accomplish?

- Clarifies that “**reimbursements**” from TRICARE to TriWest to pay TRICARE-authorized civilian health care providers (i.e., hospitals, clinics, individual physicians, and other health care providers) for medical services provided to TRICARE **beneficiaries** are exempt from the general excise tax

How?

- By adding a new category of specific transactions to the “additional exemptions” section of Chapter 237 (§237-24.75)
 - The new subsection (3) will only apply to amounts received by a *managed care support contractor* of the TRICARE program . . . for *reimbursement* of costs or advances made to *health care providers* pursuant to a contract with the United States

*Will the State of Hawaii lose revenue if
SB 2155 or HB 2306 becomes law?*

- **No!**
 - GET taxes have never been paid for “reimbursements” received by a “managed care support contractor” by TriWest and predecessor contractors
 - Managed care support contractors have never been assessed GET on reimbursements
 - Don’t know nor can we explain how Dept. of Taxation arrived at \$3.6 million/yr revenue loss
 - Dept. of Taxation estimated annual reimbursements of \$90.3 million/yr=\$3.6 million GET @4% (see SSCR2375/SB 2155 SD1)
 - Note: TriWest’s annual “reimbursements” received from TRICARE are approximately \$30 million/yr.