THE STATE OF NEW HAMPSHIRE
JUDICIAL BRANCH
SUPERIOR COURT

Rockingham Superior Court
Rockingham Cty Courthouse/PO Box 1258
Kingston NH 03848-1258

Telephone: 1-855-212-1234
TTY/TDD Relay: (800) 735-2964
http://www.courts.state.nh.us

NOTICE OF DECISION

Laura Beardsley Lombardi, ESQ
NH Attorney Generals Office
33 Capitol Street
Concord NH 03301-6397

Case Name: **Northeast Rehabilitation Hospital v. New Hampshire Department of Revenue Administration**
Case Number: **218-2012-CV-00185**

Enclosed please find a copy of the court's order of February 07, 2014 relative to:

Order on Cross Motion(s) for Summary Judgment

February 07, 2014

Raymond W. Taylor
Clerk of Court

(398)

C: Mary Ann Dempsey, ESQ; Margaret H. Nelson, ESQ

The State of New Hampshire

ROCKINGHAM, SS. **SUPERIOR COURT**

Northeast Rehabilitation Hospital

v.

New Hampshire Department of Revenue Administration

Docket No. 218-2012-CV-185

ORDER ON CROSS MOTIONS FOR SUMMARY JUDGMENT

This matter comes before the Court on cross motions for summary judgment. Pursuant to RSA 21-J:28-b, IV, the petitioner, Northeast Rehabilitation Hospital, seeks review of a decision of the Department of Revenue Administration's decision, denying reconsideration of an order which declined to refund petitioner's payment of the Medicaid Enhancement Tax ("MET") for the taxable period ending on June 30, 2011. Specifically, the petitioner argues that 1) the MET is an unconstitutional double tax, 2) the Department unconstitutionally discriminated against the petitioner by taxing revenue on its outpatient services while not taxing the same services provided by other providers, and 3) the MET unconstitutionally "set up an irrational and unsustainable classification of property" in violation of the Equal Protection Clause of the Fourteenth Amendment of the United States Constitution (Pet.'s Mem. of Law Sup. Mt. for S. J., 1)[1] After reviewing the pleadings, the Court finds and rules as follows.

Facts

[1] The petitioner also argues in its motion for summary judgment that the Department discriminates against hospitals by taxing them differently than other for-profit enterprises. This argument, however, is not properly before the court because it was raised for the first time on summary judgment. Because it was not addressed in the original petition, it was not addressed in the Department's answer, and discovery may not have focused on this claim. At the beginning of this case, the revenue earned at the facilities operated by the petitioner in Massachusetts were also subject to the Department's MET. The parties agree that the State's MET cannot be imposed on those out of state revenues.

The following facts are taken from the parties' Agreed Statement of Facts. The petitioner is a for-profit corporation licensed by the state under RSA 151 as a "Special Hospital-Rehabilitation." The Department of Revenue Administration ("the Department") is the State agency charged with administering certain New Hampshire tax statutes.

In 1981, the United States Congress authorized Disproportionate Share Hospital ("DSH") payments to supplement traditional Medicaid payments for certain providers to cover costs such as uncompensated care. The payments are made directly to each state based upon a statutory formula, and contemplate a dollar-for-dollar match for State funds contributed to the DSH program. In 1991, the General Court implemented a tax on gross patient services revenue[2] for every hospital. This tax, codified at RSA 84-A, is the MET. Revenues collected from the MET were to go into The Medicaid Enhancement Fund, no less than 50 percent of which would be sent to the hospitals. The remainder of the funds collected at the end of each fiscal year laps into the State's general fund.

Among other services, the petitioner provides physical therapy, occupational therapy and speech therapy on an outpatient basis. These services, and other outpatient services, such as audiology, pain and psychology, are subject to the MET. Some of these services are also offered by non-hospital providers such as private physical therapy providers. The services are identical whether they are offered by a hospital or a non-hospital entity. The payments that these non-hospital providers receive from outpatient therapy services are not subject to the MET.

The State's Medicaid program made DSH payments by paying to each qualifying hospital a DSH amount equal to the smaller of the hospital's maximum DSH limit or the amount paid in MET. From 1992 to 2010, whenever the petitioner's calculated MET liability exceeded

[2] In 2004, this was amended to tax "net patient services revenue" which is defined as the "gross charges of the hospital less any deducted amounts for bad debts, charity care, and payor discounts." RSA 84-A:1, IV-a (Supp. 2004).

its DSH payment, the Department granted the petitioner a reduction in its MET liability to match the DSH payment. Beginning in the State's 2011 fiscal year, the formula for calculating a DSH payment to a hospital changed. See RSA 167:64, I(d) (Supp. 2009). As a result, the amount of money a hospital pays under the MET could exceed, for the first time, the amount of money a hospital received as a DSH payment.[3] Because the MET is now a real tax on the petitioner's revenue, it has marshaled its forces to defeat it. Before 2010-2011 any opinions that the petitioner had as to the legality of the MET were not formally expressed since the Department's application of it in the past had not resulted in the loss of any revenue.

On November 29, 2010, the petitioner received a DSH payment in the amount of $1,480,632.00. For the taxable period which began on July 1, 2010 and ended on June 30, 2011, the MET taxed all general hospitals, and special rehabilitation hospitals that received DRG[4] payments at a rate of 5.5% of their net patient services revenue. The petitioner paid $1,480,632.00 in MET on November 19, 2010.

The petitioner, being a for-profit corporation, also pays the Business Profits Tax ("BPT") under RSA 77-A. While there is no explicit credit for the BPT under the MET, and no explicit credit for the MET under the BPT, the BPT, as a profits tax, uses a federal calculation as its baseline which allows for the deductions of certain taxes. The deductions and credits allowed under the two taxes differ.

On February 11, 2011, the petitioner filed a timely refund request with the Department, seeking a full refund of the MET, arguing that facially and as applied, RSA 84-A violated the

[3] Previously, some hospitals might not even put the MET on their books because the State would wire a DSH payment to the hospital and the hospital would quickly wire the same amount back for the MET.
[4] Prior to 2011, only hospitals which received Medicaid diagnosis related group ("DRG") payments had to pay the MET, but the law has been amended to remove that condition.

State and Federal constitutions. This request was denied. On May 2, 2011, the petitioner filed a petition for reconsideration. This petition was also denied.

Analysis

"[W]hether or not a statute is constitutional is a question of law." Cloutier v. State, 163 N.H. 445, 451 (2012). A court will only declare a statute unconstitutional when "a clear and substantial conflict exists between it and the constitution." State v. Hollenback, 164 N.H. 154, 157 (2012). Summary judgment is proper "if pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits filed, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." RSA 491:8-a, III. The parties agree, and the Court finds, that there are no genuine issues of material fact. Accordingly, this case can be decided based solely on the cross motions for summary judgment. The Court will address each argument in turn.

I. The MET is or is not an Unconstitutional Double Tax

"It is a fundamental principle in taxation that the same property shall not be subject to a double tax, payable by the same party either directly or indirectly." Phillips v. City of Concord, 145 N.H. 522, 524 (2000); see also N.H. CONST. Pt. I, Art. 12. "The dispositive inquiry in cases involving alleged double taxation is whether the two taxes are determined by separate and distinct factors." First Fin. Group of N.H. v. State, 121 N.H. 381, 386 (1981) (citations and quotations omitted). In resolving this inquiry, the Court must look at the nature of the two taxes involved to "determine whether the two schemes of taxation are based on separate and distinct factors." Id. at 387.

The Court finds First Fin. Group instructive in this case. In that case, the plaintiff was the principle of a bank, and objected to paying the business profits tax and a bank tax under RSA 84

(repealed 1993). Id. at 385. In deciding that there was no unconstitutional double tax, the New Hampshire Supreme Court noted "that that statute [the bank tax] does not necessarily tax the receipt of income generated by a bank. Rather, depending upon the type of bank, RSA ch. 84 imposes a tax of one percent upon the par value of the bank's capital stock. A tax is also imposed upon the interest and dividends that are paid out by the bank to its depositors. RSA ch. 84 does not tax the bank's business profits." Id. at 387 (citations omitted). Although "both tax a cash stream passing through a bank, the taxes are not identical" because one taxes the corporation's profits and the other taxes the bank's stock and dividends. Id.

In the case at bar, the BPT taxes the petitioner's profits, while the MET taxes net revenue.[5] Moreover, the taxes allow for different credits and deductions. The BPT taxes economic gain—it starts with gross receipts but allows deductions for, among other things, compensation to officers, salaraies and wages, repairs and maintenance, rent, advertising, licensing, and depreciation. By contrast, the MET taxes economic volume. This distinction persuades the Court that the schemes of taxation focus on distinct and separate factors. See Opinion of the Justices, 111 N.H. 136, 140 (1971) (holding, in a different context that "the characteristics of gross income are sufficiently distinct from those of net income as to admit of separate classification.") In the Department's memorandum of law, the following appears: "When the substance of the two taxes is examined, it becomes clear that the calculation of 'net patient services revenue' ('NPSR') for the purposes of the MET is 'sufficiently distinct' from the calculation of 'total income' for purposes of the BPT, such that there is a meaningful and real difference between the classes of property being taxed." (Dept.'s Mem., 13.) The Court agrees.

[5] Net revenue is not the same as profit. Profits are "[t]he excess of gross sales over cost of goods plus expenses of operation." BALLENTINE'S LAW DICTIONARY (William S. Anderson ed., 3rd ed. 1969). By contrast, net patient services revenue is the "gross charges of the hospital less any deducted amounts for bad debts, charity care, and payor discounts." RSA 84-A:1, IV-a (Supp. 2004).

II. The Application of the MET to the Petitioner's Outpatient Services Permissibly or Impermissibly Classifies the Taxpayer

In analyzing whether a tax impermissibly classifies a taxpayer, the Court must determine "whether the *same* class of property is being taxed differently so that taxpayers who ought to be treated equally are in fact being subjected to disparate schemes of taxation and to differing tax burdens." Opinion of the Justices, 123 N.H. 296, 307 (1983) (emphasis in the original). Put succinctly: "Property can be classified for tax purposes. The taxpayers cannot." Opinion of the Justices, 106 N.H. 202, 205 (1965) (citations and quotations omitted).

The petitioner claims that the MET impermissibly classifies taxpayers because identical services are taxed differently, depending on the provider. For example, a hospital-owned speech therapy practice would have to pay the MET on its revenues, while a privately owned speech therapy clinic would not, even though the services provided are the same. The Department counters that "[t]he MET is not a tax on therapist services. It is a tax on revenue derived from the provision of *inpatient hospital services* and *outpatient hospital services*." (Resp.'s Mem., 18) (emphasis in the original). As such, the Department argues, the statute classifies property, and not taxpayers. Thus, if there is a reasonable basis for the classification, the Department continues, the Court must uphold the scheme.[6]

A close look at the statute and rules reveals that the statutory scheme does indeed impermissibly classify taxpayers. "Net patient services revenue means the gross charges of the hospital less any deducted amounts for bad debts, charity care, and payor discounts[,]" including outpatient hospital services. RSA 84-A, IV-a. Indeed, the only difference between "therapist

[6] The Department also argues in its reply that "the MET is similar to other New Hampshire statutes which tax revenue derived from a certain type of service that can only be provided by a certain type of entity." (Resp.'s Reply, n5.) In this case, however, the service can be provided by other types of entities—namely non-hospital affiliated providers.

services" and "outpatient hospital services," is elucidated in the Departments' Rule Rev-2301.08(c)—namely that to provide outpatient hospital services, one must be a hospital. See N.H. Admin. Rules, Rev-2301.08 ("Outpatient hospital services means preventive, diagnostic, therapeutic, rehabilitative, or palliative services that: (a) Are furnished to outpatients; (b) Are furnished by or under the direction of a physician or dentist; and (c) Are furnished by an institution that: (1) Is licensed or formally approved as a hospital by an officially designated authority for State standard setting; and (2) Meets the requirements for participation in medicare [sic] as a hospital."). It is a distinction without a difference. That the MET also covers other revenue does not change the underlying problem—the petitioner is paying tax on revenue, that, if the petitioner were not a hospital, it would not have to.

In short, the Court agrees with the petitioner on this issue. The petitioner is forced to pay the MET on its outpatient therapy services while other, non-hospital, providers of identical services are not. There could be two identical physical therapy offices next door to each other, providing identical services, and if one was owned by a hospital and the other was not, they would be taxed differently. This is an unconstitutional classification of taxpayers. See Opinion of the Justices, 106 N.H. at 206 (presuming unconstitutionality of scheme where "[p]hysicians self-employed would be taxed, while those performing like services for the state or a private employer would be free of taxation.").

III. The Petitioner's Claim that the Classification of Taxpayers violates the Equal Protection Clause

The petitioner next argues that "RSA 84-A violates the Fourteenth Amendment to the United States Constitution. . . because the taxpayer and property classifications described above are not rationally related to any legitimate State interest." (Pet.'s Mem., 18.) The Court has

already found that taxing therapy services provided by hospitals while not taxing identical services provided by hospitals is unconstitutional. Therefore because the Court has found that the Department's classification is irrational, it also finds that the MET deprives the petitioners of the Equal Protection of the Federal Constitution both facially and as applied.

Conclusion

For the reasons discussed above, the petitioner's motion for summary judgment is GRANTED IN PART and DENIED IN PART. The Department's motion for summary judgment is GRANTED IN PART and DENIED IN PART. The Court holds that the MET is not an unconstitutional double tax, but as related to outpatient services is an unconstitutional classification of taxpayers. The petitioner is therefore entitled to a refund for the portion of the MET paid on revenue derived from any outpatient services which are not subject to the MET when provided by non-hospital entities.

So Ordered.

February 7, 2014
Date:

Kenneth R. McHugh
Presiding Justice