PUBLICATION

The Battle over Medicare's Treatment of Provider Taxes May be Coming to an End

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For much of the past decade, hospitals and CMS have battled over whether providers may claim, as Medicare reasonable costs, the full amount of provider tax assessments levied upon them by the states in which they operate. In 2011, CMS issued a "clarification" in the Provider Reimbursement Manual, (PRM) stating that while taxes may generally be allowable, providers may treat only the "net tax expense" as a reasonable cost. PRM § 2127.7. Essentially adopting the position that certain Medicare contractors had been asserting, CMS then said that the providers' tax costs must be reduced by payments received from the states and "associated with the assessed tax." Additionally, even predating the PRM change, CMS maintained in litigation that when taxes are placed by a state into a fund, and monies in that fund are used, at least in part, to make state hospital payments (such as Medicaid payments), those state payments operate in essence as "refunds" of the taxes and thus reduce the amounts that are appropriately reimbursable as Medicare costs.

Hospitals have challenged CMS's position but have been largely unsuccessful. The United States Courts of Appeals for the Seventh, Eighth and Sixth Circuits have all ruled in favor of the government. *See Abraham Lincoln Mem'l Hosp. v. Sebelius*, 698 F.3d 536, 550 (7th Cir. 2012); *Kindred Hospitals East, LLC v. Sebelius*, 694 F.3d 924 (8th Cir. 2012); *Breckinridge Health, Inc. v. Price,* 859 F.3d 422 (6th Cir. 2017). Providers, however, continued to hold out hope based on a decision from the United States District Court for the District of Columbia, *Dana-Farber Cancer Inst. v. Burwell*, 216 F.3d 49 (D.D.C. 2016). In that case, the District Court largely sided with Dana-Farber concluding that, under Medicare's regulations at 42 C.F.R. § 413.98, a refund and an expense have a "temporal and substantive relationship" such that "the amount paid back" must be for a "previous expense" to reduce a "related expense." The District Court concluded that Massachusetts fund payments to Dana-Farber were made to reduce the hospital's costs for providing care to under- and uninsured patients, and not to reduce the expense of the hospital tax.

The Court of Appeals, however, has now reversed the District Court's decision. *Dana-Farber Cancer Inst. v. Hargan*, Case No. 16-5379 (Dec. 22, 2017) The D.C. Circuit ruled that the question before it was whether the interpretation by the Provider Reimbursement Review Board (PRRB) of the refund regulation was arbitrary and capricious, and it concluded that the interpretation was not. The court determined that the provider tax was imposed to generate revenues for a Massachusetts fund that was then used to make hospital payments, thereby making the tax and payments "inextricably linked." The court further ruled that the PRRB had reasonably focused on the guiding principal of statutory and regulatory language instructing that Medicare reimbursement is permitted only for costs "actually incurred."

Baker Donelson Comments

The impact of this latest decision is significant. With rulings from four United States Courts of Appeals, including the most recent ruling from the D.C. Circuit, and with no decisions to the contrary, providers that might wish to challenge CMS's Medicare provider tax policy may now be hesitant to do so. Unless the structure of the provider tax program in a particular state is so unlike those programs that have previously been the source of litigation, it seems unlikely that a reviewing court will spend much time reexamining the rationale of the prior rulings. And given the expense and effort involved in further pursuing the issue, providers may decide that their efforts are better spent elsewhere.