

01-035

TAXATION: LICENSE TAXES.

Exception to federal preemption applies to local license tax levied on businesses participating in TRICARE health insurance program because tax is imposed on broad range of business activity and not solely on cost of individual health care benefits.

The Honorable Ross A. Mugler
Commissioner of the Revenue for the City of Hampton
October 31, 2001

You ask whether federal law preempts the authority of a locality to levy a local business license tax on businesses participating in the TRICARE health insurance program.

You relate that a local company is a prime contractor under a Department of Defense managed health care support contract referred to as TRICARE. You also relate that the company has contracted with another local company to fulfill certain administrative duties pertinent to the TRICARE contract. You further relate that the first company has stated that it is an insurer and the second company has stated that it is not an insurer. You note that neither company is subject to taxation under Chapter 25 of Title 58.1 of the *Code of Virginia*, which subjects insurance companies to state license taxation.¹ You inquire whether federal law preempts local business license taxation of such companies.

The TRICARE program provides health insurance for military personnel and their dependents and was designed by the Department of Defense to reduce costs for the military hospital system through a regionalized managed care program.² The federal regulations establishing the TRICARE program are contained in 32 C.F.R. § 199.17 (2000). With respect to preemption, § 199.17(a)(7)(i) generally preempts state and local laws "relating to health insurance, prepaid health plans, or other health care delivery or financing methods." Accordingly, § 199.17(a)(7)(ii) directs that any state or local law "relating to health insurance, prepaid health plans, or other health care delivery or financing methods is preempted and does not apply in connection with TRICARE regional contracts." Importantly, § 199.17(a)(7)(iii) provides:

Preemption, however, does not apply to taxes, fees, or other payments on net income or profit realized by such entities in the

conduct of business relating to [Department of Defense] health services contracts, if those taxes, fees or other payments are applicable to a broad range of business activity.

Regarding the preemption of state and/or local laws by federal law, it is important to note that § 199.17(a)(7) is not a blanket preemption of state or local laws; rather, it sets forth, in detail, when state and local laws are preempted by the federal law and when they are not. "Congress' enactment of a provision defining the pre-emptive reach of a statute implies that matters beyond that reach are not pre-empted."³ Thus, the preemption provisions of § 199.17(a)(7) apply only to state or local laws articulated in such section whereas state or local laws which come within the exception designated in § 199.17(a)(7)(iii) are not preempted.

The primary goal of statutory construction is to discern and give effect to legislative intent.⁴ In examining § 199.17(a)(7), paragraphs (a)(7)(i) and (ii) provide for preemption of state and local laws relating to "health insurance, prepaid health plans, *or other health care delivery or financing methods.*" (Emphasis added.) This language indicates the intent of Congress to preempt state or local laws which impact methods of providing health care services through TRICARE. Section 199.17(a)(7)(iii), however, in providing that preemption does not apply to "taxes, fees, or other payments on net income or profit realized," so long as such "taxes, fees, or other payments are applicable to a broad range of business activity," indicates Congress' intent to distinguish between laws specifically affecting the provision of health care and laws reflecting a broader business application.

It is my opinion that a local business license tax comes within the purview of § 199.17(a)(7)(iii), and is not preempted. Significantly, paragraph (a)(7)(iii) also provides that, for the purpose of assessing the effect of federal preemption of state and local taxes regarding Department of Defense health services contracts, interpretations must be consistent with § 8909(f) of the Federal Employees Health Benefits Program.⁵

Similar to § 199.17(a)(7), § 8909(f)(1) prohibits the imposition by a state or locality of any "tax, fee, or other monetary payment . . . , directly or indirectly, on a carrier or an underwriting or plan administration subcontractor" of the Federal Employees Health Benefits Program with respect to payments made from the Employees Health Benefits Fund. Section 8909(f)(2) provides that

[p]aragraph (1) shall not be construed to exempt any carrier or underwriting or plan

administration subcontractor ... from the imposition ... of a tax, fee, or other monetary payment on the net income or profit accruing to or realized by such carrier or underwriting or plan administration subcontractor ..., if that tax, fee, or payment is applicable to a broad range of business activity.

The court decisions under § 8909(f) have not dealt specifically with a local business license tax; however, they are instructive in determining whether such a tax is intended to be preempted by federal law.

In the case of *Health Maintenance Organization of New Jersey v. Whitman*, the State of New Jersey imposed an assessment on certain health insurance carriers which was used to defray financial losses incurred by those carriers who provided a disproportionate share of higher-risk individual health insurance coverage.⁶ The court held that, since the assessment had the effect of increasing the cost of individual health care benefits, such assessment was preempted by § 8909(f).⁷ In so holding, the court found that, because the assessment was imposed only on the hospital services industry, it was not imposed on a broad range of business activity as would preclude preemption pursuant to § 8909(f)(2).⁸ The court noted that, for a tax, fee, or monetary payment to apply to a broad range of business activity, it must, at the very least, apply to more than a single industry.⁹

In the case of *Connecticut v. United States*, the State of Connecticut imposed a six percent sales tax on hospital charges for patient care services which was paid into the state's general fund and a one percent "provider tax" on hospitals' gross earnings.¹⁰ The court held that these taxes were not preempted by § 8909(f).¹¹ Regarding the sales tax, the court found that the tax was applied and administered in conformity with the state's general sales tax and thus was applicable to the broad range of business activity exception provided in § 8909(f)(2).¹² With respect to the provider tax, the court determined that, because the tax was assessed on gross earnings of hospitals and was paid into the state's general fund, it, too, was not preempted by § 8909(f).¹³

Unlike the tax at issue in *Whitman*, the local business license tax is not a singular tax applicable to one industry; rather, it is applicable to a multitude of businesses.¹⁴ In addition, it is not a tax assessed on or relative to the cost of individual health care benefits, as was the tax at issue in *Whitman*. Like the taxes at issue in *Connecticut*, the local business license tax is uniformly assessed on a broad range of business activity.¹⁵ Accordingly, the local business license tax is a general tax imposed on

businesses rather than a tax unique or specific to the financing or delivery methods of health insurance carriers.

Therefore, it is my opinion that the local business license tax comes within the purview of 32 C.F.R. § 199.17(a)(7)(iii) and is thus not preempted.

¹Note that § 58.1-3703(C)(11) exempts from local license taxation insurance companies subject to taxation under Chapter 25 of Title 58.1.

²*Schism v. United States*, 972 F. Supp. 1398, 1407 (N.D. Fla. 1997).

³*Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 517 (1992).

⁴*Turner v. Commonwealth*, 226 Va. 456, 459, 309 S.E.2d 337, 338 (1983).

⁵5 U.S.C. § 8909 (1994).

⁶72 F.3d 1123 (3rd Cir. 1995).

⁷*Id.*

⁸*Id.*

⁹*Id.* at 1132.

¹⁰1 F. Supp. 2d 147, 150 (D. Conn. 1998).

¹¹*Id.* at 153.

¹²*Id.*

¹³*Id.*

¹⁴See § 58.1-3703(A) (authorizing counties, cities, and towns to impose license tax on "businesses, trades, professions, occupations and callings and upon the persons, firms and corporations engaged therein").

¹⁵*Id.*

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