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NO. 97557-4

IN THE SUPREME COURT  
OF THE STATE OF WASHINGTON

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PEACEHEALTH ST. JOSEPH MEDICAL CENTER AND  
PEACEHEALTH ST. JOHN MEDICAL CENTER,

Appellants,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent.

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APPELLANTS' ANSWER TO AMICUS CURIAE MEMORANDA ON  
THE MERITS

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## I. INTRODUCTION

On April 22, 2020, this Court granted two motions for leave to file amicus curiae memoranda on the merits in this case. The memoranda of (1) the Washington State Hospital Association (“WSHA”) and (2) Seattle Children’s Hospital and Seattle Cancer Care Alliance (“SCH/SCCA”) as amici curiae were therefore filed. The Court granted the parties an opportunity to file answers to the amicus memoranda not later than May 11, 2020.

By filing this answer, Appellants (“PeaceHealth”) hereby adopt the arguments and authorities set out in the amicus memoranda. PeaceHealth also answers (1) that the amicus briefs both appropriately emphasize how the legislative intent provision of the 2002 enactment of RCW 82.04.4311 gives meaning to the disputed clause in question, and that the intent statement has more weight than a typical statement of legislative purpose because it spoke to the constitutionality of the enactment, and (2) the amicus memoranda highlight in important additional ways why the Department’s interpretation of RCW 82.04.4311 lacks any justification under controlling precedents applying the Commerce Clause of the United States Constitution, art. I, § 8, cl. 3.

## II. ARGUMENT

### A. Both Amicus Memoranda Accurately Identify the Legislature's Intent to Cover All Federally Supported Hospital Care Services, Including Other States' Medicaid and Children's Health Programs.

The amicus memoranda are united in refuting the Department's pinched view of the importance and meaning of the legislative statement of intent in Section 1 of 2002 Laws, ch. 314.

The intent statement bears a repeat quotation:

The legislature finds that the provision of health services to those people who receive *federal or state subsidized health care benefits* by reason of age, disability, or lack of income is a *recognized, necessary, and vital governmental function*. As a result, the legislature finds that it would be inconsistent with that governmental function to tax amounts received by a public hospital or nonprofit hospital qualifying as a health and social welfare organization, when the amounts are paid under a health service program subsidized by federal or state government.

2002 Laws, ch. 314, sec. 1 (emphasis added).

As WSHA points out, “[i]t is undisputed that Medicaid payments from every state are subsidized by the federal government.” Amicus Curiae Memorandum of the Washington State Hospital Association (“WSHA Merits Br.”) at 3. WSHA correctly argues that other states’ Medicaid programs, subsidized by the federal government, are just as much within the Legislature’s scope of concern as is Medicare.

SCH/SCCA argue that the “legislative findings ‘serve[] as an important guide in understanding the intended effect of operative sections.’” Brief of Amici Curiae Seattle Children’s Hospital and Seattle Cancer Care Alliance (“SCH/SCCA Merits Br.”) at 6 (quoting *Hartman v. Wash. State Game Comm’n*, 85 Wash.2d 176, 179, 532 P.2d 614 (1975)). They point out that the breadth of the legislative intention to relieve community hospitals of tax on “federal or state subsidized health care benefits” sheds light on the specific structure of the deduction statute and the language in dispute in this case. That is, of the three clauses in RCW 82.04.4311, two are expressly delimited to a federal and to a state health program, respectively (“federal medicare” and “the state of Washington basic health plan”), whereas the clause in dispute in this case addresses “medical assistance [and] children’s health” generically, without a parallel initial delimitation to “state of Washington” programs. *Id.* at 6-7. PeaceHealth has made a similar point. *See* Response Br. at 12-14.

Notwithstanding the Department’s attempts to minimize the importance of these legislative findings, *see* Department’s Supplemental Br. at 12, the intent statement actually has greater weight in this case than normally because the Legislature was specifically addressing a constitutional issue in the bill. Section 4 of chapter 314, 2002 Laws, provided for retroactive application of the new deduction back to

January 1, 1998. This entailed both refunds to qualifying hospitals that had paid B&O tax on federally and state-subsidized health care programs and a waiver of tax liability for hospitals that had not paid. As this Court recently reiterated, Article VIII, Section 5 of the State Constitution prohibits the State from making a gift of public funds. *Peterson v. State*, No. 97410-1, slip op. at 7 n.4, 460 P.3d 1080, 2020 WL 1888727 \*2 n.4 (Wash. Apr. 17, 2020). The Legislature’s intention to refund the previously paid taxes raised the question whether the measure would entail a prohibited gift of public funds. *See City of Yakima v. Huza*, 67 Wash.2d 351, 359, 407 P.2d 815 (1965). The intent statement in Section 1 of the bill spoke directly to this question.

“To determine whether a challenged transaction is in fact a gift of public funds, ‘[f]irst, the court asks if the funds are being expended to carry out a fundamental purpose of the government?’” *Peterson*, slip op. at 8, 2020 WL 1888727 \*3 (quoting *CLEAN v. State*, 130 Wash.2d 782, 797, 928 P.2d 1054 (1996) (citations omitted)). In Section 1 of the bill, the Legislature answered this question for the Court and the public, in effect saying, “Yes, paying these refunds supports the performance of ‘a *recognized, necessary, and vital governmental function*’ by public and nonprofit hospitals, namely, the ‘provision of health services to those people who receive *federal or state subsidized health care benefits* by

reason of age, disability, or lack of income’.” The Legislature thus rejected further reliance on the economically and constitutionally dubious intent statement in the misconceived 2001 amendments – that it sought to extend its “purchasing power,” 2001 Laws, 2d sp. sess., ch. 23, sec. 1 – because (1) the State does not purchase health care benefits for the elderly as a class, (2) relying on the purpose of extending the State’s “purchasing power,” even if economically accurate with respect to Medicaid, could not constitutionally justify refunding tax paid on federal Medicare reimbursements, and (3) the B&O tax deduction had never affected the State’s Medicaid reimbursement costs either.

For these reasons, the arguments of WSHA and SCH/SCCA that the Legislature intended to extend the deduction to all medical assistance and children’s health programs subsidized by the federal government are exactly right.

**B. The Amicus Curiae Memoranda Show the Department’s Reliance on the “Government Function” and “Market Participant” Exceptions to Commerce Clause Scrutiny Has No Economic Support.**

The amicus curiae memoranda show in detail why the Department’s claim of exemption from Commerce Clause scrutiny for its interpretation of RCW 82.04.4311 has no basis.

**1. WSHA and SCH/SCCA Show That RCW 82.04.4311, as Interpreted by the Department, Does Not Favor State Health Care Programs in the Focused Way Required by the *Davis* Case.**

First, regarding the “government function” exception adopted by the U.S. Supreme Court in *Dep’t of Revenue of Ky. v. Davis*, 553 U.S. 328, 128 S. Ct. 1801, 137 L. Ed. 2d 685 (2008), and relied on without analysis by the Court of Appeals, *see PeaceHealth St. Joseph Med. Ctr. v. State*, 9 Wash. App. 2d 775, 784, 449 P.3d 676 (2019), PeaceHealth’s prior briefing has argued that there is no predicate for the exception because the B&O tax deduction does not affect the finances of the State’s health benefits programs. *See* Response Br. at 33; *see also* AR 35-36 (PeaceHealth’s Reply in Support Mot. S.J.). The amicus memoranda add considerable detail that proves the point.

SCH/SCCA show that, while providing health care services to underserved populations is indeed a government function, imposing a tax on hospitals differentially based on the state of patient residency does not help the State compete against other “competitors,” in contrast to Kentucky’s scheme to exempt interest on its bonds from state income tax but not interest on the bonds of other issuers. SCH/SCCA Merits Br. at 14. If the Department’s position embodies any marketplace incentives, it encourages Washington community hospitals to serve the senior citizens

of Oregon, for example, under Medicare, but to avoid serving Oregon's indigent under Medicaid and CHIP if they can. The Department does not show how this result would "favor" the State's health programs.

The WSHA Merits Brief extends this analysis, showing that the Supreme Court in *Davis* endorsed Kentucky's self-favoring tax exemption because the exemption was narrowly tailored to Kentucky's role as a bond issuer. *See* WSHA Merits Br. at 4-5. If the Washington Legislature had been trying to impact its health care costs, it would not have provided the deduction for Medicare receipts in RCW 82.04.4311 or omitted for-profit hospitals in a deduction targeted at Medicaid receipts.

WSHA also calls this Court's attention to the long history of both Washington's approach to reimbursing hospitals for Medicaid services and its tax policy for nonprofit and public hospitals, and how fundamentally disconnected they are. *See* WSHA Merits Br. at 6-7. WSHA shows that the tax policy is simply regulatory, and not self-favoring. In *Davis*'s own terms, the Commerce Clause's strict scrutiny applies. *See Davis*, 553 U.S. at 338 ("A discriminatory law is 'virtually per se invalid.'") (quoting *Oregon Waste Systems, Inc. v. Dep't of Environmental Quality of Ore.*, 511 U.S. 93, 99, 114 S. Ct. 1345, 128 L. Ed. 2d 13 (1994)); *id.* at 344 (Commerce Clause scrutiny applies to discriminatory tax laws in the absence of an exception).

**2. SCH/SCCA Highlight Precedent That Undermines the Claim That a State Medicaid Program Can Ever Qualify for the “Market Participant” Exception.**

SCH/SCCA also debunk the Department’s argument that its interpretation qualifies for the “market participant” exception to Commerce Clause scrutiny. *See* SCH/SCCA Merits Br. at 15-17. Clearly, the deduction under RCW 84.04.4311 does not entail “*direct state participation in the market*” for hospital services. *Id.* at 15 (quoting, with added emphasis, *White v. Mass. Council of Constr. Emp’rs, Inc.*, 460 U.S. 204, 208, 103 S. Ct. 1042, 75 L. Ed. 2d 1 (1983) (internal quotation and citation omitted)). The whole point of the statute was to restructure tax relief for nonprofit and public hospitals in response to the fact that both federal and state programs were contracting with third parties to manage various combinations of physician, hospital, and other health care benefits.

Also, notwithstanding the Department’s reliance on the *White* decision (as SCH/SCCA point out), *White*’s analysis shows that state Medicaid programs *cannot* qualify for the “market participant” exception. In *White*, the Supreme Court endorsed the City of Boston’s preference for public-works contractors that employed at least half residents of Boston. As to contracts wholly funded with city monies, the Court held that the city was free to impose this discrimination as a market participant. As to

contracts funded in part with a federal contribution, however, the Court upheld the discrimination solely because the federal funding program affirmatively endorsed local-labor preferences. *See White*, 460 U.S. at 213-14.

Pursuant to the Commerce Clause, Congress has the power to do what states cannot. *Id.* In *White*, Congress had authorized a local preference. In the case of Medicaid, it has done the opposite. As WSHA points out, federal Medicaid regulations require that state Medicaid plans “establish procedures to facilitate the furnishing of medical services to individuals who are present in the State and are eligible for Medicaid under another State’s plan.” 42 C.F.R. § 431.52 (quoted in WSHA Merits Br. at 10). The Department has pointed to nothing in federal law that endorses a discriminatory tax policy based on residency of Medicaid beneficiaries. The Department’s interpretation does not qualify for exemption from Commerce Clause scrutiny under either *White* or *Davis*.

Ultimately, the Department’s argument about the Legislature’s intentions is a pose. The Department would have this Court believe that the Legislature wanted qualified hospitals to be able to deduct Medicare receipts regardless of the patient’s state of residency, and wanted all hospitals to pay B&O tax on compensation from private insurance or self-paying patients regardless of the patient’s state of residency, but wanted to

tax Medicaid and CHIP receipts differentially based on the patient’s residence – even though this difference has no discernible impact in promoting any aspect of Washington health programs. There is no justification for this discrimination. “[A] State ‘may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State.’” *Comptroller of the Treasury of Md. v. Wynne*, 575 U.S. 542, 135 S. Ct. 1787, 1794, 191 L. Ed. 2d 813 (2015) (quoting *Armco Inc. v. Hardesty*, 467 U.S. 638, 642, 104 S. Ct. 2620, 81 L. Ed. 2d 540 (1984)).

### III. CONCLUSION

For the above-stated reasons, this Court should reverse the decision below.

RESPECTFULLY SUBMITTED this 11th day of May, 2020.

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## CERTIFICATE OF SERVICE

I, Diane Wright, hereby certify that on the date below I electronically filed *Appellant's Answer to Amicus Curiae Memoranda on the Merits* with the Clerk of the Court using the Washington State Appellate Courts' e-file portal, which will send notification of such filing to all counsel of record at the following e-mail addresses:

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DATED at Seattle, Washington, this 11th day of May, 2020.

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