

Technical corrections were made to this notice on December 20, 2010 by Revenue Notice # 10-06. Please see Revenue Notice # 10-06 for the corrected language.

MINNESOTA DEPARTMENT OF REVENUE

Revenue Notice # 06-07: MinnesotaCare Tax – Exemptions and Credits - Research

Introduction

This revenue notice explains the difference between the research exemption under Minnesota Statutes, section 295.53, subdivision 1(a)(9), and the research credit under Minnesota Statutes, section 295.53, subdivision 4a.

Research Exemption

The research exemption excludes certain payments received for patient services from gross revenues subject to the MinnesotaCare tax. A taxpayer must use the exemption if it applies. This means that a taxpayer cannot choose to use the credit instead of the exemption.

The following principles apply to the research exemption:

- The exemption applies to payments received by hospitals, surgical centers, or health care providers from another entity (e.g., medical device manufacturer) for providing patient services that are incurred through a formal program of health care research;
- Payments received from patients or from third party payers (e.g., Medical Assistance or insurance companies that pay on behalf of a patient) are subject to tax even if the services provided were part of a research program;
- The research must be conducted in conformity with federal regulations governing research on human subjects; and
- To report qualifying receipts, hospitals, surgical centers, and health care providers must include the payments on the MinnesotaCare tax return on line 1, "Total gross receipts . . . for health-care services." These payments must then be included as an exemption on the line titled: "Amount received from sponsors of health-care research and designated by the sponsors to be applied to the cost of health-care services connected with the research, . . ." This amount is subtracted from the total amount of payments received for health care services, along with other exemptions from the tax.

Research Credit

The research credit allows hospitals and health care providers to take a credit against the total amount of the tax for expenditures used to fund qualifying research.

The following principles apply to the research credit:

- The credit applies to expenditures a health care provider or hospital incurs while performing or funding research;
- The research program must be a formal program of medical and health care research conducted by an entity that is exempt under section 501(c)(3) of the *Internal Revenue Code of 1986* or is owned and operated under authority of a governmental unit. The entity paying for the research need not meet this requirement;
- The amount of the credit must not exceed the tax liability of the hospital or health care provider;
- The credit must not be applied to payments that are not subject to tax. For example, receipts included as exemptions under *Minnesota Statutes*, section 295.53, subdivision 1, cannot be included in the research expenses used to calculate the credit;
- The entity performing the research is not required to meet the definition of a hospital or a health care provider. The entity taking the credit must meet the definition of a hospital or health care provider;
- The credit can be taken by either the entity that performs the research or by the entity that funds the research;
- Under *Minnesota Statutes*, section 295.53, subdivision 4a(e), if the estimated or actual amount paid under the credit provision exceeds \$2,500,000, the commissioner of finance shall determine the rate of the credit for the following calendar year, to the nearest one-half percent so that refunds will most closely equal \$2,500,000.

Examples (the examples reflect the 2006 2.5 percent rate of the credit)

1. Health care provider A gives health care provider B a grant to conduct qualifying research. The funds for the grant originated with Provider A's taxable revenues for patient services. The research conducted by Provider B does not involve patient services. Provider B is a 501(c)(3) entity. Provider A is a for-profit entity.

Provider A may take a credit against the tax it owes. Provider B cannot take the credit or the exemption because payments for the research in this example are not included in B's taxable receipts.

2. A 501(c)(3) health care provider receives \$300,000 for patient services. The provider reduces the gross revenue subject to the MinnesotaCare tax by \$100,000 in allowable exemptions. The amount subject to the MinnesotaCare tax is \$200,000, resulting in a tax liability of \$4,000 (2 percent of \$200,000). The provider's expenses for performing qualifying research total \$250,000 for the year.

The provider is entitled to a credit of \$4,000 (even though 2.5 percent of the research expenses is \$6,250) since the amount of the credit cannot exceed the provider's tax liability.

3. A drug company gives a hospital \$2,000 for patient services that are incidental to drug research conducted by the hospital. Patients have to make co-payments of \$10 for each visit. The hospital spends an additional \$30,000 on research.

The \$2,000 qualifies for the research exemption. The co-payments made by patients are taxable. The \$30,000 may qualify for the research credit, as long as 2.5 percent of the \$30,000 does not exceed the hospital's net MinnesotaCare tax liability. Since the co-payments are subject to tax, they are included in revenues for patient services for purposes of the credit calculation. Since the \$2,000 is not taxable, it cannot be included in the research expenses used to calculate the research credit.

4. A hospital receives \$100,000 in taxable patient receipts. The receipts do not qualify for the research exemption or any other exemption under *Minnesota Statutes*, section 295.53, subdivision 1. The hospital also receives a research grant for \$10,000. The research does not involve patient services and the grant is thus not included in the hospital's taxable patient receipts. The hospital incurs \$13,000 in expenses for conducting this research project.

The hospital is entitled to a credit of \$75 (2.5 percent of \$3,000) as follows: Of the \$13,000 of expenses incurred, \$10,000 was paid for by a grant that is not included in gross revenues for patient services. This leaves \$3,000 of expenses to be paid from revenues for patient services. Since 2.5 percent of \$3,000 does not exceed the MinnesotaCare tax, the entire \$3,000 may be used to calculate the research credit.

5. Health care provider A gives hospital B a grant to provide patient services as part of B's conducting research. The amount given to B was included in A's taxable receipts.

Health care provider A can take the research credit if it meets the requirements under *Minnesota Statutes*, section 295.53, subdivision 4a. Hospital B can take the research exemption if it meets the requirements under *Minnesota Statutes*, section 295.53, subdivision 1(a)(9). Hospital B cannot take the credit because the credit cannot be applied to payments that are not subject to tax.

JOHN H. MANSUN, Assistant Commissioner
for Tax Policy and External Relations

Publication Date: June 5, 2006