
Expert: Tax Bill has Negative Implications for Health Systems.

In December, President Donald Trump signed the Tax Cuts and Jobs Act into law, effective Jan. 1.

Much has been written about how those changes to the Internal Revenue Tax Code will affect businesses, but little has been said about how the tax bill will affect municipal, nonprofit hospitals like those in the Norman Regional Health System.

"There are some specific implications for nonprofits," said NRHS CFO Ken Hopkins, reporting on the effects of the bill to hospital authority board members Monday.

While some elements of the bill will have only minor or no affect on the health system, there are three elements of the Tax Cuts and Jobs Act that have major implications for Norman Regional.

Those three are the elimination of the individual mandate, the elimination of advance refunding bonds and the reduction in the corporate tax rate.

After failing to kill the Affordable Care Act, Republicans used the partisan-supported tax bill to weaken the ACA. The Tax Cuts and Jobs Act eliminates the individual mandate penalty for not having health insurance starting in 2019.

While the repeal of the individual mandate leaves other ACA provisions in place, the mandate was designed to control adverse selection and expand the risk pool in the individual market, Hopkins said.

The Congressional Budget Office estimates that four million people will initially lose coverage, with that number rising to 13 million people losing coverage over the next decade, while premiums may rise 10 percent as a result of the repeal.

Unlike private hospitals that can turn away people without insurance, nonprofits like the Norman Regional Health System serve everyone, regardless of their ability to pay. That means an increase in the number of uninsured people affects Norman Regional's bottom line.

Hopkins said according to Moody's, this will cause the uninsured population to rise, hurting hospital operating margins and cash flow.

Elimination of advance refunding bonds: The Tax Cuts and Jobs Act basically eliminates advance refunding for municipal bonds issued after 2017 by making interest on advance refunding bonds taxable. Hopkins said that eliminates flexibility that municipal issuers have had to take advantage of lower interest rates and raises long-term borrowing costs.

Refunding is a new bond that pays off an older, higher-interest bond to save on debt service, restructure those debts or free up funds. It's similar to a homeowner refinancing a mortgage to get a better interest rate or restructure payments and dates for budget flexibility.

Advance refunding allows entities to take advantage of low interest rates by refinancing bonds ahead of the call date, Hopkins explained to board members.

"You could borrow new money at lower rates, use those monies to give to a trustee and then they would pay off the bond holders on the old bond at the call date," Hopkins said. "But all of that happened outside our balance sheet, so we would be sitting here left with nothing but the new debt at lower rates. This is actually what we did in 2016 and 2017. A lot of what we did were advanced refundings, and we got economic gain from that."

Alternatives — such as interest rate swaps — introduce more risk, cost more and are more complex, Hopkins said.

Florida's bond finance director said his state saved $3 billion over past 10 years from advanced refunding, and locally the Norman Regional Health System saved between $33 million to $38 million in cash value savings with a net present value of $20 million to $24 million.

"This law disallows us from being able to do this in the future," Hopkins said. "That ultimately raises the borrowing costs."

Reduction in corporate tax rate: The 40 percent Reduction in the corporate rate also will affect the health system because the effective net benefit of owning municipal bonds will drop.

"We don't pay taxes, so that changing rate doesn't affect us, but what it does do is it changes the desirability of tax-exempt bonds," Hopkins said. "The reason you would purchase a tax-exempt bond is due to the tax advantage, and if the tax advantage is lessened, then the attractiveness of buying that bond in the first place is also lessened.

"The impact of lowering that rate is that the kinds of people who buy those bonds — banks and insurance companies — have to hold lots of reserves and they like to hold these bonds because of that tax advantage."

Without the advantage, tax exempt municipal bonds like Norman Regional become less attractive for bank, property and casualty insurance and life insurance companies.

Municipal bonds will have to yield more relative to taxable bonds for corporate buyers to be willing to purchase them, he said which weakens the demand for tax-exempt bonds.

"When we want to issue bonds, it could be harder to find buyers for those," Hopkins said. "One of the impacts of disallowing advance refunding is that the supply of bonds will go down. One of the impacts of lowering the rate is that the demand for bonds will go down. It may be that those two effects offset each other in terms of price, but at a much lower volume, so there's likely to be much less tax-exempt debt in the market."

Hopkins said it's hard to know every impact over time.

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