

425.0027

Memorandum

To: Mr. Rick Kinoshita (MIC:87)
Settlement Section

Date: July 18, 1995

From: John L. Waid
Tax Counsel

Subject: REDACTED TEXT

I am answering your memorandum to me dated May 18, 1995. You request our opinion as to the taxability of the taxpayer's sales of food supplements. You indicate that this taxpayer is under audit, but that a settlement offer has been received. You attached to your memorandum a copy of a draft memorandum that the auditor, Mr. Alfredo Ortiz of the REDACTED TEXT District, had proposed to send to me back in 1994, but, for unknown reasons, did not send.

You indicate that the petitioner offers its customers nutritional counseling along with the sale of the food supplements. While it sells the supplements, it is not a licensed pharmacy. Mr. Ortiz' memorandum states that the head of the taxpayer is not an M.D., but "for prescription purposes, patients are 'rung up' through a doctor REDACTED TEXT who is a doctor of medicine." You indicate that the taxpayer sells dietary supplements such as vitamins, minerals, amino acids, herbs, and similar pills (hereinafter generally referred to as "vitamins"). The chart you attached to your memorandum shows that sale of herbal pills and dietary supplements make up about 73% of its sales. Mr. Ortiz indicates that the items at issue are sold on a 100% mark-up and that these sales supply the majority of the taxpayer's revenue. There appears to be no dispute that these items are excluded from the definition of food products under Regulation 1602(a) (5).

Apparently, the proposed memorandum was shown to the taxpayer. You attached to your memorandum a copy of an undated letter entitled "To Whom It May Concern" on letterhead of Dr. REDACTED TEXT ("the letter"), signed by both Dr. REDACTED TEXT and the head of the taxpayer. A handwritten note on the letter says "Taxpayers response to proposed legal letter." The letter described the taxpayer's operation, in part, as follows:

"Our operation took advantage of an existing corporation owned by REDACTED TEXT, Ph.D., however patient care was fully overseen by Dr. REDACTED TEXT. REDACTED TEXT worked under her. No one received any nutrients without paying sales tax unless Dr. REDACTED TEXT had seen them and prescribed nutritional supplementation care.

"The nutrients prescribed were chosen on the basis of medical testing, blood, urine, etc. and on presentation of symptoms consistent with deficiency patterns well established in the literature. Patients were never given the same nutrients in the same amounts. A supplement chart was prepared for each patient and good only for a specified time period.

"Once nutrients were repleted the patients were of course recommended to stop use."

(Emphasis in original.) The letter further states that, prior to the time Dr. REDACTED TEXT became associated with it, the taxpayer paid tax on all supplement sales. Although the letter does not say so, it leaves the impression that the taxpayer operated after Dr. REDACTED TEXT became associated with it essentially as it had before then.

OPINION

We have previously determined that vitamins can be considered medicines as defined by Regulation 1591(b) (1); if so, their sales to a physician or surgeon for the treatment of a human being are exempt from tax under Regulation 1591(a) (4). (Annot. 425.0940 (7/3/64).) We have also determined that herbs and herbal products may also qualify as medicines. (Annot. 425.0410 (12/31/91).) Under the regulation, however, the "medicine" must be used in the "diagnosis, cure, mitigation, treatment or prevention of disease." As a result, vitamins and herbs are deemed medicines only when they are sold for the purpose of treating a specific medical condition. Sales of vitamins merely to regulate vitamin intake would not be generally recognized as a medical purpose. (Reg. 1591(b) (1).) The same logic applies to the amino acid and the "similar" pills.

You do not indicate the nature of the taxpayer other than to say that it offers its patrons "nutritional counseling," and its letter does not describe any diseases from which its patients were suffering. The letter does list certain diseases which are caused by vitamin deficiencies, but does not say that its clients were suffering from any of those diseases. The taxpayer is also not apparently operating as a hospital or any other medical facility. Therefore, we conclude that the taxpayer is not treating its clients for any kind of medical condition, i.e. one that a doctor would have to treat. We find especially significant the phrase in the letter regarding stopping supplement use once the clients' "nutrients were repleted." This appears more related to the correction of nutrition deficiencies than to treatment of a disease. Thus, we conclude, based on the facts as we have them here, that the vitamins do not qualify as "medicines" as that term is defined in Regulation 1591(b) (1).

The letter refers, however, to "presentation of symptoms consistent with deficiency patterns well established in the literature." There thus may be an argument that some, at least, of the vitamins are in fact sold to treat specific diseases and thus qualify as medicines under the above authority. Even if they are considered medicines, though, their sales are not exempt unless made pursuant to the requirements of Regulation 1591(a) (1-4), subdivision (a) (5) is not applicable. You note that the taxpayer is not a registered pharmacy, so (1) is out. We have noted that the taxpayer does not appear to be a health facility as defined in the regulation, so the sales of these items would not qualify under (3). You state that the taxpayer sells the vitamins, and the letter indicates that it is an entity separate from Dr. REDACTED TEXT. It is most likely the taxpayer that is purchasing the items. They are thus not sold to a licensed physician or health facility so subdivision (4) does not apply.

Could the vitamins be considered to be sold or furnished by Dr. REDACTED TEXT herself so that subdivision (a)(2) would apply? They are, as noted above, sold to the customers at retail by the taxpayer as the major source of its revenue. Although we have previously determined that sales by a doctor's professional corporation are the same as sales by the doctor personally, it is clear that Mr. REDACTED TEXT, and not Dr. REDACTED TEXT owns the taxpayer. We conclude that the taxpayer is selling the items at issue as the major portion of its business. Regulation 1591(a)(2) covers transfers of medicines from the hands of the doctor

directly to the patient. Sales by a health facility or pharmacy are covered by other subdivisions. Thus, we conclude that, since the taxpayer, and not Dr. REDACTED TEXT is furnishing the items at issue, such sales are not exempt under subdivision (2). Dr. REDACTED TEXT may possibly hand out or otherwise directly furnish some of the items at issue, probably mostly as samples, directly to some of the taxpayer's clients herself; if so, such transfers would be exempt from tax under subdivision (2). We would expect this amount to be small.

Should this case be settled? The letter is quite right when it states that diseases such as scurvy and beri-beri are caused by vitamin deficiencies. Another is rickets. However, these diseases are exceedingly rare in the United States--so rare as to make it highly unlikely that the taxpayer's clients have them. Such diseases would have to be treated in a hospital anyway. The taxpayer may be able to demonstrate that it does sell some of its vitamins for the treatment of specific diseases. If so, under the annotations, the vitamins would be considered medicines in those instances. The medical exemption is two-pronged, however, and both the nature of the item as a medicine and the proper method of sale or use must be satisfied for the exemption to be applicable. We have concluded that the taxpayer and not Dr. REDACTED TEXT is buying and selling the vitamins, and the taxpayer is not a registered pharmacy. As a result, none of the conditions of Regulation 1591(a) are met. Based on the facts as we have them, the medical exemption does not appear to be available.

The letter states that the taxpayer got an opinion from a private attorney before associating with Dr. REDACTED TEXT. This case thus appears to be one in which a taxpayer selling vitamins in taxable transactions associated itself with a medical doctor in order to try to exempt its sales from tax. The facts and the law seem to be pretty strong on the side of the Board. The record does not indicate settlement is appropriate.

JLW:sr

Cc: REDACTED TEXT District Administrator