

This letter discusses sales of prescription drugs by servicemen. See 86 Ill. Adm. Code Part 140. (This is a GIL.)

March 1, 2010

Dear Xxxxx:

This letter is in response to your letter dated January 11, 2010, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

ABC is a long term care pharmacy that provides medication to skilled facilities and nursing homes. We have recently acquired a contract with an Illinois facility and are looking for clarification on Illinois sales tax regulations. My understanding is that all prescriptions and over the counter items are subject to sales tax in Illinois.

We adjudicate a large portion of our claims to insurance plans, including government sponsored Medicare part D plans. Private insurance companies remit payment to us on behalf of the Medicare system.

1. Do we need to obtain exempt numbers from the insurance companies in order to not charge sales tax?
2. Are Medicare part D plans subject to sales tax in Illinois?
3. We have several circumstances in which the insurance company will pay a portion of the prescription drug cost however they will impose a co pay on the patient. Are the co pay amounts that are charged to the patient subject to sales tax?

Clarification on the above mentioned questions would be greatly appreciated. Please feel free to contact me if any further information is needed.

DEPARTMENT'S RESPONSE:

Pharmacists who sell prescription drugs to customers are considered to be servicemen under the Service Occupation Tax Act.

Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on the cost price if they are registered de minimis servicemen; or, (4) Use Tax on the cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See 86 Ill. Adm. Code 140.101(f). This class of registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen do not have the option of determining whether they are de minimis using a transaction-by-transaction basis. See 86 Ill. Adm. Code 140.109.

You have indicated that you sell prescription drugs to insurance companies, including Medicare Part D sponsored programs, and purchasers who pay co-pays. It is possible you may sell prescription drugs to long-term care facilities that provide the drugs to residents as part of the resident's monthly fee or a Medicare per diem. We do not have enough information about how these

sales are transacted to respond specifically regarding the taxability of each situation; however, we hope the following information is helpful.

In general, sales made to Medicare and Medicaid are exempt from tax as sales to a government body so long as the exemption is properly documented through provision of an active exemption identification number (“E” number). See 86 Ill. Adm. Code 130.2080(a). While no tax may be due on payments made directly to vendors by Medicare or Medicaid, tax is due upon any portion of the bill paid by individuals or private insurance companies not covered by Medicare and Medicaid. This means when Medicare directly pays 80% of the medical bill and the remaining 20% is billed to the patient or his insurance company, assuming proper documentation of the exemption, the 80% is tax exempt as a governmental payment while the 20% is taxable. In the case of an unregistered de minimis serviceman, (see the final method above), he or she may take a pass through of the exemption when selling to Medicare or Medicaid. Such servicemen will still owe Use Tax on the portion of the cost billed to the patient. See 86 Ill. Adm. Code 140.108(a)(2)(A) and 86 Ill. Adm. Code 140.108(a)(2)(B).

The Medicare Part D Prescription Plan is organized differently. The government provides funds on a per capita basis to the Prescription Drug Providers (“PDPs”). The PDPs operate as private insurance companies under contract with the government. They, not the government, are responsible for purchasing drugs for their beneficiaries. The beneficiaries usually pay a co-pay. Since sales are made to the PDPs and not directly to the government, the drug sales do not qualify for the government tax exemption. Therefore sales of drugs are not exempt from tax under the Medicare D Plan. Please note that according to the U.S. Department of Health and Human Services, sales tax cannot be added to a beneficiary’s co-payment under the Plan. As a result, sales tax is due on drugs sold under the Medicare Part D Plan, but it may not be charged to the beneficiary.

If tangible personal property is not sold for use or consumption, but rather, for resale, the seller may accept a Certificate of Resale from the purchaser. No tax is imposed on a sale of property purchased for resale. Illinois law requires a Certificate of Resale to contain the information set out in 86 Ill. Adm. Code 130.1405(b). An example of a sale for resale might be if you sell prescription drugs to a long term care facility, and the long term care facility sells them to their residents as part of the residents’ monthly fee. Again, unregistered de minimis servicemen may not give a certificate of resale. They must pay the Use Tax to their suppliers.

Please note that there is also an exemption for prescription and non prescription medicines and drugs sold for use by a person receiving medical assistance under Article 5 of the Illinois Public Aid Code who reside in a licensed long-term care facility, as defined in the Nursing Home Care Act. See 35 ILCS 115/3-5(13).

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department’s Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters
Associate Counsel

RSW:mzk