

**TENNESSEE DEPARTMENT OF REVENUE
REVENUE RULING #97-06**

WARNING

Revenue rulings are not binding on the Department. This presentation of the ruling in a redacted form is information only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Departmental policy.

SUBJECT

Applicability of sales and use tax for medical supplies and services.

SCOPE

Revenue rulings are statements regarding the substantive application of law and statements of procedure that affect the rights and duties of taxpayers and other members of the public. Revenue rulings are advisory in nature and are not binding on the Department.

FACTS

The taxpayer is a Tennessee hospital ("Hospital") that is exempt from both federal income taxes, pursuant to Internal Revenue Code ("IRC") § 501(c)(3), and from Tennessee sales and use taxes, pursuant to Tenn. Code Ann. § 67-6-322. Hospital has a Division ("Division") which is licensed in accordance with Tennessee law as a home health care provider. Division's services involve providing intravenous ("I.V.") therapy to individuals. As part of its home health care program, and in addition to providing home health care services to individuals, Division sells to other home health care organizations prescription drugs and medicine, medical equipment, and supplies for administering I.V. therapy.

Under its home health care program, Division offers three different packages:

Package 1: Division's nurses are the exclusive source of the patient's I.V. therapy skilled nursing care. Division's nurses administer the I.V. therapy. In addition, a Division nurse -- other than the nurse who regularly visits the patient's home -- supervises the patient's condition by telephone or, as

needed, by personal visit. Division bills the patient or the patient's insurance company for all components of the therapy.

Package 2: Patients receive their primary skilled nursing care from another home health care provider. Patients receive from Division I.V. therapy prescription drugs and medication, medical equipment, and supplies. Division's nurses supervise the administration of the home I.V. therapy by telephone conferences with the patient. Division's nurses also supervise the home I.V. therapy by regularly receiving and reviewing nursing notes from the other home health care provider to ensure that the quality of the I.V. therapy being provided is satisfactory. Division's nurses have on occasion made visits to patients' homes when the therapy was not achieving the therapeutic goals. Such visits are not routine. However, at least once per month (and at least once during the course of therapy lasting less than one month), Division's nurses evaluate and discuss the progress of the therapy and the condition of the patient with the other agency. Division bills the patient or the patient's insurance company for the prescribed drugs along with an inclusive per-diem amount that covers the cost of equipment, supplies, nonprescription medications and staff time.

Package 3: Division sells prescription drugs and medicine, medical equipment and supplies for administering I.V. therapy to other home health care providers who administer and supervise the I.V. therapy. The other home health care providers are billed for the prescription drugs and medicine, medical equipment and supplies.

The following are the types of I.V. therapy that are administered either by Division or by the home health care providers that purchase prescription drugs and medicine, medical equipment and supplies from Division:

Total Parenteral Nutrition: The I.V. therapy provides essential vitamins, fats, sugars and amino acids to patients who are unable to feed themselves.

Hydration: The I.V. therapy enables fluid levels to return to normal when patient is unable to ingest sufficient liquids.

Antibiotic and Antifungal Treatment: The I.V. therapy administers prescribed medication to enable the body to combat disease.

Pain Management: For patients with incurable diseases, this I.V. therapy allows the patient to control the level of narcotics needed to minimize their pain because the body can no longer protect itself.

Immune: The I.V. therapy administers prescribed drugs to bolster the human immune system.

Blood Transfusions: The I.V. therapy administers blood and blood products to patients.

Chemotherapy: The I.V. therapy administers prescribed drugs to rid the body of cancer.

In all of the packages, the patient's physician prescribes the I.V. therapy. In all of the packages, the prescribed medication is prepared by Division's licensed pharmacists using the I.V. home infusion supplies and medications prescribed by the physician. In Packages 1 and 2, Division delivers the prescribed medication to the patient's home. In Packages 1 and 2, Division's nurses assess the patient's responsiveness and the effectiveness of the treatment, and supervise the patient's care by conferring with the patient and by reviewing the nursing notes of nurses of another home health care provider actually administering the I.V. therapy to the patient and conferring with the other home health care providers. In Package 3, Division has no role in the administration or supervision of the care of the patient.

ISSUES

1. Whether Division is exempt from sales and use taxes on purchases of tangible personal property and taxable services made by it in connection with its provision of health care services under each of Packages 1, 2 and 3.
2. Whether Division is required to collect sales or use tax on the services, prescription drugs and medicine, medical equipment and supplies used or consumed in Package 1.
3. Whether Division is required to collect sales or use tax on the prescription drugs and medicine, medical equipment and supplies used or consumed in Package 2.
4. Whether Division is required to collect sales or use tax on its sale of the prescription drugs and medicine, medical equipment and supplies sold in Package 3, including the following items:
 - a. prescription drugs and medicines issued by a Division pharmacist
 - b. I.V. solutions
 - c. insulin
 - d. hypodermic needles
 - e. insulin pumps
 - f. blood and blood plasma
 - g. enteral and parenteral nutrition and hydration
 - h. enteral and parenteral nutrition systems
 - i. I.V. sets, consisting of an I.V. pole, an I.V. pump, and a primary pump set

- j. I.V. and angiographic catheters, including peripheral inserted central catheters, short-term central venous peripheral lines, and Hickman catheters
- k. various component parts of I.V. supplies and equipment including batteries, extension sets, male adapter plugs, cloth adhesive tape, needles, and syringes.

RULINGS

1. Division is exempt from both sales and use tax on purchases of tangible personal property and taxable services made by it in connection with its provision of health care services under each of Packages 1, 2 and 3.
2. Division is not required to collect sales or use tax on the sale of services, prescription drugs and medicine, medical equipment and supplies used or consumed in Package 1.
3. Division is not required to collect sales or use tax on the sale of prescription drugs and medicine, medical equipment and supplies used or consumed in Package 2.
4. Division is not required to collect sales or use tax on its sale of the prescription drugs and medicine sold in Package 3. Division must collect sales tax on certain medical equipment and supplies used or consumed in Package 3 subject to the exceptions for specific equipment or entities noted below.

ANALYSIS

1. Purchases

Division purchases prescription drugs and medicine, medical equipment and supplies for all three of its Packages.

Tenn. Code Ann. § 67-6-322(a)(8) exempts from sales and use tax "tangible personal property or taxable services sold, given, or donated to any . . . hospitals" and provides in subsection (b) that the exemption applies to "such other institutions and organizations which have received a determination of exemption from the Internal Revenue Service under Section 501(c)(3) . . . of the Internal Revenue Code and are currently operating under it"

Hospital has received a determination of exemption from the Internal Revenue Service under § 501(c)(3) of the Internal Revenue Code. Hospital's divisions, including Division, operate under that federal tax exemption. Therefore, under Tenn. Code Ann. § 67-6-322, any otherwise taxable tangible personal property or services purchased by Division in

connection with its provision of health care services for each of its packages are exempt from Tennessee sales and use tax.

2. *Package 1*

In Package 1, Division bills the patient or insurance company for its services, including I.V. therapy, medicine, prescription drugs, medical equipment, and supplies. Division does not sell specific products or supplies to the patient, but sells its services. As provided in Tenn. Code Ann. §§67-6-102(23)(F), 67-6-212 and 67-6-342, only certain services are subject to the Tennessee sales and use tax. Although medical services are not specifically exempted from sales and use taxes, medical services are not among those services on which the tax is imposed. Thus, regardless of the circumstances under which medical services are sold, Division will not be required to collect sales tax. As stated above, Division is not required to pay tax on its purchases, including the materials used in the provision of Package 1.

To the extent that charges to the patient or insurance company include rental charges for equipment, Division's IRC § 501(3)(c) status does not exempt it from collecting tax. Tenn. Code Ann. § 67-6-352 provides, in pertinent part, that "home health care providers engaged in the business of rendering outpatient health care services to human beings are the consumers or users of all tangible personal property or taxable services purchased for . . . rental in providing the health care service." Based on the facts provided, Division is a licensed home health care organization which provides health care services as defined in Tenn. Code Ann. § 68-11-201(15). Since Division is a home health care provider, it is the user and consumer of tangible personal property which it rents to other entities or people. As a result, Division will not have to collect tax on its rental of items used in conjunction with providing health care services.

3. *Package 2*

In Package 2, Division bills the patient or insurance company for prescribed drugs and an inclusive per diem amount covering the cost of equipment for I.V. therapy, supplies, nonprescription medications, and staff time. As the provider of health care services in Package 2, Division is the ultimate user or consumer of any products it uses in conjunction with Package 2. Tenn. Code Ann. § 67-6-352. As stated above, Division's exemption under IRC 501(c)(3) applies and Division is exempt from paying tax on items it purchases for use in providing home health care in Package 2.

The per diem amount for Division's services, which include the use of equipment and supplies, is not subject to tax. Accordingly, Division is not required to collect tax for the provision of Package 2.

4. *Package 3*

In Package 3, Division does not provide health care services, but sells prescription drugs and medicine, medical equipment, and supplies for I.V. therapy to other home health care providers. Tenn. Code Ann. § 67-6-352 states that a home health care provider is the user or consumer of “all tangible personal property or taxable services purchased for use, consumption, or rental in providing the health care service.” Division acts only as the seller of “tangible personal property not otherwise exempt from tax [and] must collect from the . . . home health care provider the appropriate tax, unless the pharmacy or home health care provider is exempt from paying the sales or use tax under § 67-6-322.” Division, a dealer as defined in Tenn. Code Ann. § 67-6-102(6)(C), only sells tangible personal property and is not the user or consumer of the medicine, equipment, or supplies.

The home health care purchaser of the items is the user or consumer and in accordance with § 67-6-352, is liable for the use tax unless otherwise exempted. Division must collect tax from the home health care providers who are not otherwise exempt through an IRC § 501(c)(3) exemption. Even if the purchasing home health care organization does not qualify for the IRC § 501(c)(3) exemption, however, tax will only be due on the sale of items not otherwise exempt from tax. Many of the items sold by Division are exempt from tax, as stated below.

a. Prescription Drugs and Medicines issued by a Division Pharmacist.

These sales are exempt pursuant to Tenn. Code Ann. § 67-6-320:

- (a) There is exempt from the tax imposed by this chapter any prescription drug or medicine issued by a licensed pharmacist in accordance with an individual prescription written for the use of a human being by a practitioner of the healing arts licensed by the state of Tennessee.
- (b) There is also exempt from the tax imposed by this chapter any prescribed drug or medicine sold to a practitioner of the healing arts licensed by the state of Tennessee or issued by a licensed pharmacist for use in the treatment of a human being.

Division’s sales of prescription drugs and medicine to other home health care providers are issued by a licensed pharmacist for use in the treatment of human beings and are accordingly exempt from tax.

b. I.V. Solutions.

The types of I.V. therapy sold by Division are more fully described in the facts. The I.V. solutions are prepared by Division’s licensed pharmacists using the I.V. home infusion supplies and medications prescribed by the patient’s physician. To the extent that these solutions constitute “prescribed drugs or medicines” within the meaning of Tenn. Code Ann. § 67-6-320, the solutions are exempt from tax.

A physician may "prescribe" products that are not "prescription" drugs or medicines, but by its terms, Tenn. Code Ann. § 67-6-320 only exempts prescribed drugs or medicines from the sales tax. *Feldman v. Huddleston*, 912 S.W.2d 161 (Tenn. App.1995). In order to qualify for the exemption afforded prescription drugs, the I.V. solutions must first, in fact, be a drug or medication. The term "drug" is not defined within the sales and use tax code. The Tennessee Food, Drug and Cosmetics Act defines drug to mean "[a]rticles intended for use in the diagnosis, cure, mitigation, treatment or prevention of disease in man or other animals." Tenn. Code Ann. § 53-1-102(9)(B). Accordingly, provided that the solutions are drugs within the scope of Tenn. Code Ann. § 53-1-102(9)(B), they are exempt from tax.

c. Insulin.

The retail sale of insulin is exempt from tax as specifically provided in Tenn. Code Ann. § 67-6-312.

d. Hypodermic Needles.

Sales of hypodermic needles are generally subject to tax. The sale of hypodermic needles for use in dispensing insulin is exempt from sales and use taxes. Tenn. Code Ann. § 67-6-312.

e. Insulin Pumps.

These are used to pump insulin into the patient's body. Insulin is a hormone normally secreted by the pancreas that is essential in regulating the metabolism of sugar. When a patient's body does not naturally produce the required amount of insulin, insulin must be artificially introduced into the body.

Tenn. Code Ann. § 67-6-314(5) provides an exemption for prosthetic devices. A device is prosthetic if it is an artificial part which substitutes for or augments the performance of a natural function. *Cordis Corp. v. Taylor*, 762 S.W.2d 138 (Tenn. 1988). The insulin pump is a device necessary for artificial correction of the natural insulin deficiency and constitutes a prosthetic device within the meaning and construction of Tenn. Code Ann. § 67-6-314(5). Accordingly, the sale of such pumps are exempt from sales and use tax.

f. Blood and Blood Plasma.

Tenn. Code Ann. § 67-6-304 exempts blood and blood plasma from tax when sold by an organization with a determination of exemption from the Internal Revenue Service under IRC § 501(C)(3). exemption. Since Division operates under a § 501(c)(3) exemption, Division's sales of blood and blood plasma are exempt.

g. Enteral and Parenteral Nutrition and Hydration.

In enteral and parenteral nutrition therapy and hydration therapy, the I.V. administers essential vitamins, fats, sugars, amino acids, and fluids to patients who are either unable to feed themselves or ingest sufficient liquids. As stated above with respect to I.V. solutions, the formula or medication given to the patient through the I.V. is exempt only

if deemed a prescription drug and obtained pursuant to a prescription as provided by Tenn. Code Ann. § 67-6-320(a) or (b).

h. Enteral and Parenteral Nutrition Systems.

The systems consist of various pieces of equipment, including enteral pumps, I.V. poles, feeding bags, and tubes, used to introduce food to a patient who is unable to swallow and/or digest food normally. Enteral and parenteral nutrition systems have been deemed prosthetic devices by the Davidson County Chancery Court in *Nutritional Support Services v. Commissioner of Revenue*, (No. 88-788-II). Tenn. Code Ann. § 67-6-314(5). Bags, tubing, and any other disposable medical supplies coming into direct contact with a prescription drug or medicine administered by I.V. are also exempt pursuant to Tenn. Code Ann. § 67-6-320(c).

The exemption for I.V. systems as a prosthetic device is limited to those circumstances in which the patient cannot swallow or otherwise ingest fluids or food. As stated above, the solutions themselves will only be exempt if they constitute a “prescription drug or medicine.” Tenn. Code Ann. § 67-6-320.

i. I.V. Sets, consisting of an I.V. Pole, an I.V. Pump, and a Primary Pump Set. I.V. poles are normally not exempt. However, I.V. poles that are a necessary part of equipment that replaces or augments a bodily function, as stated above, would be exempt as a part of a prosthetic device: when the fluid being supplied artificially corrects a deficiency in the body's production of the fluid, as occurs in immune therapy and blood transfusion therapy, or where the sets are used to administer parenteral nutrition and hydration to patients unable to eat, swallow, or digest foods and liquids. Tenn. Code Ann. § 67-6-314(5); *Nutritional Support Services v. Commissioner of Revenue*, (Davidson County Chancery Court, No. 88-788-II). Otherwise, if the pole or pump does not come into direct contact with the prescription drug, it is not exempt under Tenn. Code Ann. § 67-6-320(c).

j. I.V. and Angiographic Catheters, including Peripheral Inserted Central Catheters, Short-term Central Venous Peripheral Lines, and Hickman Catheters. To the extent that any of these items are part of a prosthetic device or equipment necessary to augment or replace a body function, they are exempt from tax under Tenn. Code Ann. § 67-6-314(5). Otherwise, these items are exempt to the extent that they are “disposable medical supplies . . . dispensed by a licensed pharmacist . . . which are used for the intravenous administration of any prescription drug or medicine and which come into direct contact with the prescription drug or medicine.” Tenn. Code Ann. § 67-6-320(c). If neither exemption applies, the items are subject to tax.

k. Various component parts of I.V. Supplies and Equipment including Batteries, Extension Sets, Male Adapter Plugs, Cloth Adhesive Tape, Needles, and Syringes.

Disposable items used with prescribed I.V., such as bags, tubing, needles, and syringes, and which come into direct contact with the prescription drug or medicine, are specifically exempt from tax under Tenn. Code Ann. § 67-6-320(c). Batteries and cloth

adhesive tape do not come into direct contact with the prescribed drugs or medicine and are not exempt from tax. Extension sets, needles, and syringes, however, do come into direct contact and are exempt under this provision.

If any of the items constitutes a necessary part of a prosthetic device, it would be exempt pursuant to Tenn. Code Ann. § 67-6-314(5). Component parts of I.V. equipment and supplies which are not disposable and not otherwise part of a prosthetic device or equipment necessary to augment or replace a body function are not exempt from tax. As stated above, if the purchasing entity operates under an IRC § 501(c)(3) exemption, then Division will not be required to collect sales tax on the sale of any of the products.

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