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House Bill 4831 (as passed by the House)
Sponsor: Representative Lisa Posthumus Lyons
House Committee: Tax Policy
Senate Committee: Finance

Date Completed: 10-29-13

CONTENT

The bill would amend the General Sales Tax Act to provide a tax exemption for the sale of over-the-counter drugs pursuant to a prescription.

Currently, the sales tax does not apply to sales of drugs for human use that can only be legally dispensed by prescription. The bill, instead, would exempt the sale of a prescription drug for human use, and an over-the-counter drug for human use pursuant to a prescription.

The bill would define "prescription" and "prescription drug" as those terms are defined in Part 177 of the Public Health Code.

(The Code defines "prescription" as an order by a prescriber (e.g., a licensed dentist, physician, or podiatrist) to fill, compound, or dispense a drug or device written and signed; written or created in an electronic format, signed, and transmitted by facsimile; or transmitted electronically or by other means of communication.

"Prescription drug" means one or more of the following:

- A drug dispensed pursuant to a prescription.
- A drug bearing the Federal legend "CAUTION: federal law prohibits dispensing without prescription" or "Rx only".
- A drug designated by the Michigan Board of Pharmacy as a drug that may only be dispensed pursuant to a prescription.)

MCL 205.54g

BACKGROUND

Michigan's sales tax exemption for prescription drugs is found both in statute and in the State Constitution, although the statutory provisions and the constitutional language are not identical. Article IX, Section 8 of the Constitution provides, "No sales tax or use tax shall be charged or collected...on the sale or use of prescription drugs for human use." Accordingly, both the Use Tax Act and the General Sales Tax Act contain an exemption for the sale of prescription drugs. Previously, the exemption in each Act applied to purchases or sales of "a prescription drug for human use", using virtually the same language as in the Constitution.

Amendments enacted in June 2004, however, changed the language exempting sales or purchases of prescription drugs. Each Act now exempts sales of "drugs for human use that can *only* be legally dispensed by prescription" (emphasis added).

These amendments responded to a March 2004 decision of Michigan Court of Appeals concerning the exemption in the Use Tax Act (*Birchwood Manor, Inc. v Commissioner of Revenue*, 261 Mich App 248). Three nursing homes had challenged the Revenue Commissioner's assessment of the use tax on their purchase of over-the-counter drugs that were dispensed by licensed pharmacists pursuant to prescriptions written by physicians. The Court of Appeals held that the OTC drugs *were* exempt from the use tax under the exemption for purchases of "a prescription drug for human use".

The Court stated, "Though the statutory provision appears to broaden the tax exemption contained in the Constitution, the Michigan Legislature has the right to further define and expand the definition of 'prescription drug' in order to implement the constitutional mandate. Furthermore, if the Legislature wished to exempt only those drugs that can be purchased only with a doctor's prescription, it could have easily said so in the statute."

The Court pointed out that this holding had additional support in the Public Health Code's definition of "prescription drug", which includes a "drug dispensed pursuant to a prescription".

As a result of the 2004 amendments, a drug that can be both purchased over the counter *and* prescribed by a physician (such as ibuprofen) is not eligible for the statutory exemption.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill would reduce sales tax revenue by approximately \$12.8 million per year, assuming that physicians provide prescriptions for roughly 30% of sales most likely to be associated with a prescription. The actual reduction would depend on the extent to which consumers request, and physicians supply, prescriptions for over-the-counter drugs. Because sales tax revenue is distributed to different funds and expenditures, under the above assumption the bill would annually reduce School Aid Fund revenue by \$9.4 million, General Fund revenue by \$2.1 million, and constitutional revenue sharing to cities, villages, and townships by \$1.3 million.

Fiscal Analyst: David Zin

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