

Legislative Analysis



SALES AND USE TAX EXEMPTIONS FOR OVER-THE-COUNTER DRUGS WITH PRESCRIPTION

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House Bill 4464 (reported from committee as H-1)

House Bill 4465 (reported from committee as H-1)

Sponsor: Rep. Lisa Posthumus Lyons

Committee: Tax Policy

(Enacted as Public Acts 171 & 172 of 2015)

Complete to 5-11-15

Analysis available at
<http://www.legislature.mi.gov>

BRIEF SUMMARY: House Bills 4464 and 4465 alter the Sales and Use Tax Acts, respectively, to facilitate the implementation of a tax exemption for the sale of over-the-counter drugs for human use dispensed with a prescription.

House Bill 4464 changes the definition of an over-the-counter (OTC) drug in Section 4g of the General Sales Tax Act (MCL 205.54g); House Bill 4465 specifically exempts the sales of OTC drugs with a prescription from taxation under the Use Tax Act.

Both bills, as substituted in committee, are retroactive to March 14, 2014.

FISCAL IMPACT: As written, the bills would have no new fiscal impact because the bills are codifying current practice. Public Act 211 of 2013 (or House Bill 4831 from the previous legislative session) provided the sales tax exemption for over-the-counter drugs dispensed with a prescription. However, without an accompanying use tax amendment (as now being provided by House Bill 4465), use tax would be owed on these products instead. Unlike the sales tax, which is collected by the retailer at the point of purchase, the use tax is owed by the purchaser, and is therefore unlikely to have been remitted.

THE APPARENT PROBLEM:

The state constitution has exempted sales of prescription drugs for human use from the sales and use taxes since 1975. This exemption was implemented by amendments to the General Sales Tax Act and the Use Tax Act. Those amendments applied to sales of "drugs for human use that can only be legally dispensed by prescription." Subsequently, Public Act 211 of 2013 exempted over-the-counter (OTC) drugs dispensed with a prescription from the sales tax; however, the legislature did not provide a similar exemption from the use tax. Without also exempting OTC drugs from the use tax, they remain subject to tax, which was not the intent of PA 211. Also, the definition of OTC drugs in current law needs to be amended for clarity and conformity.

THE CONTENT OF THE BILL:

House Bill 4464 alters the existing language in Section 4g, and exempts from the sales tax both OTC drugs dispensed by prescription and drugs only available legally by prescription. The existing language defines what is a "prescription" and a "prescription drug," but does not define "over-the-counter" drugs. The language in HB 4464 strikes the definitions of

"prescription" and "prescription drug," and then defines OTC drugs as "a drug that is labeled in accordance with the format and content requirements required for labeling over-the-counter drugs under 21 CFR 201.66." The requirements referred to are those laid out by the federal Food and Drug Administration.

The new language replaces the previous definition for "prescription drug," and refers instead to drugs for human use that "can only be legally dispensed by prescription" and exempting them from the sales tax. These drugs are exempt from taxation under the state constitution. The language of HB 4464 is consistent with the language of this section of the Sales Tax Act before it was amended by Public Act 211 of 2013.

House Bill 4465 alters Section 4d of the Use Tax Act (MCL 205.94d) to exempt the sales of over-the-counter drugs with a prescription from the use tax. OTC drugs are defined by the same FDA labeling standard as in HB 4464. Without this companion use tax exemption, the sales tax exemption for OTC drugs simply makes the sale subject to the use tax. This has been the case since Public Act 211 of 2013 took effect on March 14, 2014. By adding OTC drugs to the list of use tax exemptions, sales of these drugs to consumers will now be fully exempt from taxation.

Committee substitutes (H-1) for both HB 4464 and 4465 make the bills retroactive to May 14, 2014, the effective date of PA 211 of 2013.

ARGUMENTS:

For:

The Michigan Constitution exempts prescription drugs for human use from the sales/use tax. (This was added to the constitution by voter initiative, along with food.) While in the past this may have covered all drugs dispensed with a prescription from a doctor, changes in the market have given consumers the option of obtaining a prescription from a physician for drugs that can be sold over-the-counter. Public Act 211 of 2013 exempted OTC drugs dispensed with a prescription from the sales tax in order to conform to what some believe is the intent of the exemption in the constitution; namely, to exempt medically necessary products. By adding the use tax amendment and making clarifying definitions, House Bills 4464 & 4465 will fully realize the intended exemption created by PA 211 and make it retroactive to the effective date of PA 211 (March 14, 2014).

Response:

Sales tax exemptions disproportionately affect the School Aid Fund. The SAF has been subject to a multitude of tax cuts in recent years. By cutting the sales tax base with the exemption for OTC drugs, these bills would reduce the amount of money available to educate the children of this state year after year. While it is true that these bills simply implement the legislature's intent from Public Act 211 of 2013, the exemption could arguably be limited to drugs that can only be dispensed with a prescription rather than also include OTC drugs for which a patient is able to obtain a prescription, and still meet the requirements of the constitutional exemption.

POSITIONS:

The Department of Treasury indicated support for the bills. (4-29-15)

A representative of the Michigan Pharmacists Association indicated support. (4-29-15)

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