

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-00(32)S
Sales Tax
September 7, 2000

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S000424A

On April 24, 2000, the Department of Taxation and Finance received a Petition for Advisory Opinion from Underberg & Kessler LLP, 1800 Chase Square, Rochester, New York, 14604.

The issues raised by Petitioner, Underberg & Kessler LLP, are whether certain purchases and sales as described below are exempt from sales and compensating use tax as purchases made for resale or as sales of prosthetic aids.

Petitioner submitted the following facts as a basis for this Advisory Opinion.

A professional corporation ("PC") performs dental services for compensation. The PC is considering two alternate business structures for operating a dental lab to manufacture dentures, partial dentures, bridges, artificial teeth and crowns. The dental lab will operate either as a division of the PC or as a single-member LLC, wholly owned by the PC. The two business structures are described as follows:

Business Structure #1

The dental lab would be a division of the PC. The PC will purchase precious metals, porcelain and acrylics both for the repairing of teeth and for the dental lab to use in the manufacture of prosthetic aids. The PC would issue resale certificates to vendors, but only for the material to be incorporated into the prosthetic aids.

Business Structure #2

The PC would transfer the assets necessary to operate the dental lab to a newly formed single-member LLC in exchange for all of the membership interest in the LLC. The LLC will purchase precious metals, porcelain and acrylics to manufacture prosthetic aids and issue resale certificates to the vendors. The LLC would not provide dental services for compensation or purchase materials as an agent of the PC. After manufacture, the LLC will sell the prosthetic aids to the PC.

Applicable Law and Regulations

Section 1101(b)(4)(i) of the Tax Law defines retail sale as "A sale of tangible personal property to any person for any purpose, other than (A) for resale as such or as a physical component part of tangible personal property, or (B) for use by that person in performing the services subject

to tax under paragraphs (1), (2), (3), (5), (7) and (8) of subdivision (c) of section eleven hundred five where the property so sold becomes a physical component part of the property upon which the services are performed or where the property so sold is later actually transferred to the purchaser of the service in conjunction with the performance of the service subject to tax....

Section 1105 of the Tax Law provides, in part:

On and after June first, nineteen hundred seventy-one, there is hereby imposed and there shall be paid a tax of four percent upon:

(a) The receipts from every retail sale of tangible personal property, except as otherwise provided in this article.

Section 1115(a) of the Tax Law provides, in part:

Receipts from the following shall be exempt from the tax on retail sales imposed under subdivision (a) of section eleven hundred five and the compensating use tax imposed under section eleven hundred ten:

* * *

(3) Drugs and medicines intended for use, internally or externally, in the cure, mitigation, treatment or prevention of illnesses or diseases in human beings, medical equipment (including component parts thereof) and supplies required for such use or to correct or alleviate physical incapacity, and products consumed by humans for the preservation of health but not including cosmetics or toilet articles notwithstanding the presence of medicinal ingredients therein or medical equipment (including component parts thereof) and supplies, other than such drugs and medicines, purchased at retail for use in performing medical and similar services for compensation.

(4) Prosthetic aids, hearing aids, eyeglasses and artificial devices and component parts thereof purchased to correct or alleviate physical incapacity in human beings.

Section 526.6 of the Sales and Use Tax Regulations provides, in part:

(a) The term retail sale or sale at retail means the sale of tangible personal property to any person for any purpose, except as specifically excluded.

* * *

(c) Resale exclusion. (1) Where a person, in the course of his business operations, purchases tangible personal property or services which he intends to sell, either in the form in which purchased, or as a component part of other property or services, the property or services which he has purchased will be considered as purchased for resale, and therefore not subject to tax until he has transferred the property to his customer.

(2) A sale for resale will be recognized only if the vendor receives a properly completed resale certificate. See sections 532.4 and 532.6 of this Title.

Section 528.4 of the Sales and Use Tax Regulations provides, in part:

(a) Exemption. (1) Drugs and medicines intended for the use, internally or externally in the cure, mitigation, treatment or prevention of illnesses or diseases in human beings, medical equipment (including component parts thereof) and supplies required for such use or to correct or alleviate physical incapacity, and products consumed by humans for the preservation of health are exempt.

* * *

(h) Taxable medical equipment and supplies. (1) Medical equipment and supplies purchased for use in performing medical or similar services for compensation are not exempt from tax.

* * *

Example 4: Dental supplies such as porcelain, mercalloy, gold, silver, acrylic denture base, amalgam, composite resin, silicate, and dental floss are not exempt when purchased by a dentist who will use them in performing a dental service for compensation.

(2) Medical services for human beings include but are not limited to the practices of medicine, dentistry, physical therapy, chiropractic, nursing, podiatry, optometry and radiology, whether performed by a private practitioner, clinical laboratory, hospital, nursing home, ambulance service, clinic, or health maintenance facilities.

Section 528.5 of the Sales and Use Tax Regulations provides, in part:

(a) Exemption. Prosthetic aids, hearing aids, eyeglasses and artificial devices and components thereof, purchased to correct or alleviate physical incapacity in human beings are exempt from the tax.

(b) Qualifications. (1) In order to qualify as a prosthetic aid, a hearing aid, eyeglasses or an artificial device, the property must either completely or partially replace a missing body part or the function of a permanently inoperative or permanently malfunctioning body part and must be primarily and customarily used for such purposes and not be generally useful in the absence of illness, injury or physical incapacity.

Example 1: Artificial hands, arms, legs, false teeth, etc. are exempt.

* * *

Example 4: A crown which is permanently attached to a tooth by a dentist is exempt.

Opinion

Business Structure #1

In Business Structure #1, the dental lab is a division of the PC. The PC will purchase the named materials for both the repairing of teeth in the course of providing the medical services of dentistry and for the manufacture of prosthetic aids such as dentures, bridges, artificial teeth and crowns by the dental lab. The PC will furnish the prosthetic aids that it manufactures to its patients in conjunction with the medical services.

In Dental Society of State of N.Y. v. N.Y.S. Tax Comm., 110 A.D. 2d 988, affd. 66 N.Y.2d 939 the Appellate Division reversed a lower court's ruling which held that gold, silver and other alloys and substances used in repairing teeth "qualified for an exemption as prosthetic aids and held that the implementing regulation, 20 NYCRR 528.4(h), relied on by defendant was invalid." The Appellate Division stated, in part:

Special Term essentially concluded that since the subject materials are utilized to make both false teeth and crowns, which are expressly exempt, so necessarily must be the component parts. This conclusion is in direct conflict with the Department's regulation interpreting the statutory exemption for drugs and medicines, set forth in Tax Law § 1115(a)(3),... Nor can we agree with plaintiff's contention that the distinction between crowns and false teeth, which are exempt, and filling substances, which are not, is irrational. Raw materials can be rationally

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distinguished from equipment (Matter of Slattery Assoc. v Tully, 79 AD2d 761, 762, affd 54 NY2d 711). In construing the meaning of “prosthetic aid”, we search for “an accommodation between a common understanding of the term and the legislative purpose” (Engle v Talarico, supra, p 241). The ordinary, commonsense meaning of prosthesis is an artificial device used to replace a missing part of the body (see, Webster’s Third New International Dictionary 1822 [P. Gove ed. 1961]).

The PC performs medical services for compensation within the meaning and intent of Section 1115(a)(3) of the Tax Law and Section 528.4(h)(2) of the Sales and Use Tax Regulations. The precious metals, porcelain and acrylics purchased by the PC are for use in performing nontaxable medical services, and therefore, are purchased at retail, whether they are used for the repair of teeth or to make a prosthetic aid. Accordingly, the PC may not use a resale certificate when it purchases such materials for use in performing nontaxable medical services.

Based on The Dental Society of the State of New York, supra, and in accordance with Section 1115(a)(3) of the Tax Law and Section 528.4(h) of the Sales and Use Tax Regulations, the purchase by the PC of the materials as described in Business Structure #1 for use in performing medical services for compensation are subject to sales and compensating use tax.

Business Structure #2

In Business Structure #2, the PC will form an LLC by transferring the assets comprising the dental lab to the single-member LLC. In exchange for the transfer of such assets the PC will receive 100% of the ownership interest in the LLC. Under Business Structure #2, the LLC will purchase materials necessary to manufacture prosthetic aids and then will sell such prosthetic aids to the PC. When the LLC purchases such materials it plans on issuing resale certificates to the vendors who sell the materials to the LLC. The LLC is treated as a partnership separate from the PC. When the PC transfers assets to the LLC upon its organization in exchange for an interest therein, such transfer is not a retail sale subject to tax. (See Deloitte & Touche, LLP, Adv Op Comm T&F, January 30, 1998, TSB-A-98(2)S).

In Alvy Dental Supply Co., Adv Op Comm T&F, July 17, 1995, TSB-A-95(27)S, the Petitioner was a corporation that sold tangible personal property to dental laboratories for use to manufacture dentures and crowns for resale to dentists. The tangible personal property sold included teeth, porcelain, certain acrylics and certain metals which become physical component parts of dentures and crowns, and items such as waxes, abrasives and plaster which do not. The opinion stated that “Sales by Petitioner to dental laboratories of teeth, porcelain, certain acrylics and certain metals which become a physical component part of a denture for sale by the laboratory may be purchased for resale provided the purchaser thereof gives the seller a properly completed Resale Certificate (Form ST-120) in accordance with the provisions of Section 1101(b)(4)(i) of the Sales Tax Law and sections 526.6(c)(1) and (2) of the Sales and Use Tax Regulations.”

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In accordance with Section 1101(b)(4)(i) of the Tax Law, there is no sales and compensating use tax imposed upon the purchase by the LLC of the precious metals, porcelain and acrylics incorporated into the prosthetic aids that the LLC sells to the PC as described in the facts of the Petition. Such materials are purchased by the LLC for resale. See Alvy Dental Supply Co., supra. Also, the sale of prosthetic aids by the LLC to the PC is exempt under Section 1115(a)(4) of the Tax Law. However, if the LLC sells raw materials such as the precious metals, porcelain and acrylics to the PC for use in performing nontaxable medical services, such sale constitutes a retail sale subject to sales and use tax, whether such materials are used to repair teeth or to make a prosthetic aid.

DATED: September 7, 2000

/s/
John W. Bartlett
Deputy Director
Technical Services Division

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.