STATE OF NEW MEXICO
ADMINISTRATIVE HEARINGS OFFICE
TAX ADMINISTRATION ACT

IN THE MATTER OF THE PROTEST OF
JAY, JAN C., D.O.M., PC, **No. 16-03**
TO ASSESSMENT ISSUED UNDER
LETTER ID NO. L0044230608

DECISION AND ORDER

A formal hearing on the above-referenced protest was held on January 14, 2016 before Hearing Officer Dee Dee Hoxie. The Taxation and Revenue Department (Department) was represented by Ms. Elena Morgan, Staff Attorney. Mr. Tom Dillon, Auditor, also appeared on behalf of the Department. The Taxpayer failed to appear by ten minutes past the scheduled time. A brief record was made at that time. Dr. Jan Jay (Taxpayer) appeared with her CPA, Mr. Terry Zelin, and witnesses, Dr. Joseph Jares, and Dr. Glenn Wilcox on January 15, 2016. The hearing was originally set for January 15, 2016, but had been moved to January 14, 2016. The Taxpayer explained that she had not received the amended notice. The Hearings Office called the Department's attorney, and Ms. Morgan and Mr. Dillon appeared again for the hearing on January 15, 2016. The Department's courtesy and professionalism was appreciated. The Hearing Officer took notice of all documents in the administrative file. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. On January 12, 2015, the Department assessed the Taxpayer for gross receipts tax, penalty, and interest for the tax periods from January 31, 2008 through December 31, 2013. The assessment was for $7,277.78 tax, $1,455.53 penalty, and $470.70 interest.
2. On April 9, 2015, the Taxpayer filed a formal protest letter.

3. On June 8, 2015, the Department filed a Request for Hearing asking that the Taxpayer's protest be scheduled for a formal administrative hearing.

4. On June 8, 2015, the Hearings Office issued a notice of hearing for a telephonic scheduling hearing. The hearing date was set within ninety days of the protest.

5. On June 24, 2015, a telephonic scheduling hearing was conducted. On June 29, 2015, a scheduling order and notice of hearing was issued.

6. On September 25, 2015, the Taxpayer filed a motion for continuance of the hearing.

7. On October 23, 2015, the order granting the motion and resetting the hearing for January 15, 2016 was issued.

8. On December 18, 2015, the Hearings Office sent amended notices of hearing resetting the hearing for January 14, 2016.

9. The Taxpayer is a doctor of oriental medicine with an expanded scope license, which allows her to prescribe certain hormones to her patients.

10. During the tax periods in question, the Taxpayer was regularly prescribing a certain dietary supplement, usually in the form of a wafer or a powder (the protein powder), to her patients as part of a treatment plan for obesity.

11. The protein powder was a proprietary formula that the manufacturers only distributed through licensed medical professionals.

12. Patients taking the protein powder needed constant medical supervision due to the possibility of ketoacidosis.

13. None of the protein powder's ingredients are a controlled substance or legally require a prescription before they may be distributed. The ingredients consist of various food

substances, some of which are milk protein concentrate, cocoa, sugar, soy protein isolate, whey protein concentrate, palm kernel oil, chocolate, and sea salt.

14. The Taxpayer was deducting from gross receipts the sales of the protein powder to her patients as she believed that the protein powder was a "prescription drug".

15. The Department audited the Taxpayer and disallowed the deductions on the sales of the protein powder as it does not include a controlled substance and is not a "prescription drug".

DISCUSSION

The issue to be decided is whether the Taxpayer was able to deduct the sales of the protein powder as a prescription drug from her gross receipts.

Burden of Proof.

Assessments by the Department are presumed to be correct. *See* NMSA 1978, § 7-1-17. Tax includes, by definition, the amount of tax principal imposed and, unless the context otherwise requires, "the amount of any interest or civil penalty relating thereto." NMSA 1978, § 7-1-3. *See also El Centro Villa Nursing Ctr. v. Taxation and Revenue Department*, 1989-NMCA-070, 108 N.M. 795. Therefore, the assessment issued to the Taxpayer is presumed to be correct, and it is the Taxpayer's burden to present evidence and legal argument to show that she is entitled to an abatement.

The burden is on the Taxpayer to prove that she is entitled to an exemption or deduction. *See Public Services Co. v. N.M. Taxation and Revenue Dep't.*, 2007-NMCA-050, ¶ 32, 141 N.M. 520. *See also Till v. Jones*, 1972-NMCA-046, 83 N.M. 743. "Where an exemption or deduction from tax is claimed, the statute must be construed strictly in favor of the taxing authority, the right to the exemption or deduction must be clearly and unambiguously expressed in the statute,

and the right must be clearly established by the taxpayer." *Sec. Escrow Corp. v. State Taxation and Revenue Dep't.*, 1988-NMCA-068, ¶ 8, 107 N.M. 540. *See also Wing Pawn Shop v. Taxation and Revenue Dep't.*, 1991-NMCA-024, ¶ 16, 111 N.M. 735. *See also Chavez v. Commissioner of Revenue*, 1970-NMCA-116, ¶ 7, 82 N.M. 97.

Gross Receipts Tax.

Anyone engaging in business in New Mexico is subject to the gross receipts tax. *See* NMSA 1978, § 7-9-4. Gross receipts tax applies to the total amount of money received from selling property or services. *See* NMSA 1978, § 7-9-3.5. It was undisputed that the Taxpayer was engaging in business and generally subject to the gross receipts tax.

Prescription drug deduction.

Receipts from the sale of "prescription drugs" may be deducted from gross receipts. NMSA 1978, § 7-9-73.2 (2007). "Prescription drugs" are defined in the statute. *See id.* They must meet three criteria to be considered "prescription drugs". *See id.* The first requirement is that they are a substance "dispensed by or under the supervision of a licensed pharmacist or by a physician or other person authorized under state law to do so". *Id.* The protein powder meets this criterion as it was dispensed by the Taxpayer, who was a doctor of oriental medicine.

The second requirement is that the substance is "prescribed for specified person by a person authorized under state law to prescribe the substance". *Id.* The protein powder was prescribed to specified persons by the Taxpayer. However, the protein powder contained only food substances, which do not require a person be authorized under state law to prescribe. Arguably, this means that anyone could "prescribe" such substances, so this requirement will be deemed to be satisfied.

The final requirement is that the substance be "subject to the restrictions on sale contained in Subparagraph 1 of Subsection (b) of 21 USCA 353." *Id.* The requirements of the United State Code are related to drugs that are potentially harmful or are limited by approved applications under another section of the code. *See* 21 USCS 353 (b) (1). The Taxpayer argues that the protein powder falls under the first provision of the statute. The Taxpayer argues that the protein powder is a substance that "because of its toxicity or other potentiality for harmful effect, or the method of its use, or the collateral measures necessary to its use, is not safe for use except under the supervision of a practitioner licensed by law to administer such drug". *Id.* The Taxpayer clearly established the medical necessity of continual supervision of any person taking the protein powder.

The Department argues that the Taxpayer has missed the key word "drug" in the statute. The relevant provision of the United States Code indicates that it applies to "[a] *drug* intended for use by man". *Id.* (emphasis added). The Department argues that under state and federal law food is not considered to be a drug. Food is defined in the federal statute as "(1) articles used for food or drink for man or other animals, (2) chewing gum, and (3) articles used for components of any such article." 21 USCS 321 (f). Drug is defined as well, and it includes "articles (*other than food*) intended to affect the structure or any function of the body of man or other animals" and clarifies that "food, dietary ingredient, or dietary supplement…is not a drug under clause (C) solely because the label or the labeling contains such a statement." 21 USCS 321 (g) (emphasis added).

The protein powder is more akin to a dietary supplement or food than it is to a drug. It does not appear to meet the statutory definition of "prescription drugs". *See* NMSA 1978, § 7-9-73.2. *See also* 21 USCS 353 and 21 USCS 321. Moreover, the regulations provide further

guidance of what are "prescription drugs". Items "that may be sold or dispensed for human consumption or administered to a human without a prescription" and "[i]tems that do not require a prescription, such as medical equipment, vitamins and aspirin" are not considered to be "prescription drugs". 3.2.234.10 NMAC (2010). The fact that the manufacturer of the protein powder does not sell its product except through licensed medical professionals using a prescription does not mean that a prescription is legally required. The protein powder and all its component ingredients are items that may be sold or dispensed legally without a prescription. Therefore, the protein powder is not a "prescription drug", and its sales may not be deducted from gross receipts.

Assessment of Penalty.

A taxpayer's lack of knowledge or erroneous belief that the taxpayer did not owe tax is considered to be negligence for purposes of assessment of penalty. *See Tiffany Const. Co., Inc. v. Bureau of Revenue*, 1976-NMCA-127, 90 N.M. 16. However, no penalty is owed when the failure to pay the tax "results from a mistake of law made in good faith and on reasonable grounds." NMSA 1978, § 7-1-69 (B). A mistake of law is a mistake about the legal effect of a known fact. *See State v. Hubble*, 2009-NMSC-014, ¶ 22, 146 N.M. 70 (quoting from dictionary). The Taxpayer made a mistake of law in deducting her sales of the protein powder. The Taxpayer's belief that the protein powder was a prescription drug was reasonable and made in good faith given the extensive evidence presented that the protein powder was used as treatment for obesity, had potentially harmful side effects, and required constant monitoring for ketoacidosis. Therefore, the penalty is hereby abated.

Assessment of Interest.

Interest "shall be paid" on taxes that are not paid on or before the date on which the tax is due. NMSA 1978, § 7-1-67 (A). The word "shall" indicates that the assessment of interest is mandatory, not discretionary. *See Marbob Energy Corp. v. N.M. Oil Conservation Comm'n.*, 2009-NMSC-013, ¶ 22, 146 N.M. 24. The assessment of interest is not designed to punish taxpayers, but to compensate the state for the time value of unpaid revenues. Because the tax was not paid when it was due, interest was properly assessed.

CONCLUSIONS OF LAW

A. The Taxpayer filed a timely written protest to the Notice of Assessment of gross receipts tax issued under Letter ID number L0044230608, and jurisdiction lies over the parties and the subject matter of this protest.

B. The protein powder sold by the Taxpayer was akin to a dietary supplement or a food item, did not require a prescription before it could be legally dispensed, and was not a prescription drug. *See* NMSA 1978, § 7-9-73.2 and 3.2.234.10 NMAC.

C. Therefore, the sales of the protein powder could not be deducted from gross receipts. *See* NMSA 1978, § 7-9-73.2.

D. The Taxpayer made a mistake of law in good faith based on reasonable grounds. Therefore, the penalty is HEREBY ABATED. *See* NMSA 1978, § 7-1-69.

For the foregoing reasons, the Taxpayer's protest **is DENIED IN PART AND GRANTED IN PART**.

DATED: February 9, 2016.

Dee Dee Hoxie

DEE DEE HOXIE
Hearing Officer
Administrative Hearings Office

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NOTICE OF RIGHT TO APPEAL

Pursuant to NMSA 1978, § 7-1-25, the parties have the right to appeal this decision by filing a notice of appeal **with the New Mexico Court of Appeals** within 30 days of the date shown above. *See* Rule 12-601 NMRA. If an appeal is not filed within 30 days, this Decision and Order will become final. A copy of the Notice of Appeal should be mailed to John Griego, P. O. Box 6400, Santa Fe, New Mexico 87502. Mr. Griego may be contacted at 505-827-0466.