

Situations in which persons who purchase pharmaceutical supplies from an exempt hospital are considered 'patients' of the hospital for purposes of determining whether the hospital is engaged in unrelated business.

The Internal Revenue Service has been requested to set forth situations in which persons who purchase pharmaceutical supplies from the pharmacy of a hospital exempt from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954 are considered 'patients' of the hospital within the meaning of section 513(a)(2) of the Code.

Section 513 of the Code defines the term 'unrelated trade or business' as any trade or business the conduct of which is not substantially related (aside from the need of an organization for income or funds or the use it makes of the profits derived) to the exercise or performance by an organization of its exempt functions. However, to the extent relevant here, section 513(a)(2) of the Code further states that such term does not include any trade or business which is carried on by an organization described in section 501(c)(3) primarily for the convenience of its patients.

In the case of a hospital exempt under section 501(c)(3) of the Code, the sale of pharmaceutical supplies by its pharmacy to persons considered 'patients' of the hospital does not constitute unrelated trade or business as defined in section 513 of the Code. See section 1.513-1(c)(2)(ii) of the Income Tax Regulations. Depending upon his relationship with the hospital, a purchaser of pharmaceutical supplies from the pharmacy of a hospital exempt from Federal income tax under section 501(c)(3) of the Code may be considered a 'patient' of the hospital as that term is used in section 513(a)(2) of the Code.

Examples of relationships that determine whether a person is a 'patient' of a hospital for purposes of section 513(a)(2) of the Code are illustrated in the six situations set out below.

Situation 1-A person admitted to a hospital as an inpatient.

A is admitted to the hospital as an inpatient. He receives bed, meals, diagnostic services, and treatment for his illness. He is a 'patient' of the hospital.

Situation 2-A person receiving general or emergency diagnostic, therapeutic, or preventive health services from outpatient facilities of a hospital.

B is taken to the hospital's emergency room for treatment of injuries sustained in an accident. He is treated in the emergency room and discharged, but is told to return to the hospital's outpatient clinic for further treatment. The hospital

maintains an outpatient clinic having regularly scheduled hours during which medical services are provided on an outpatient basis. The governing authority of the hospital has full legal responsibility for the conduct of the clinic. B visits the clinic, is registered as a patient, and receives medical care. Treatment in either the emergency room or the outpatient clinic is sufficient to make B a 'patient' of the hospital.

Situation 3-A person directly referred to the hospital's outpatient facilities by his private physician for specific diagnostic or treatment procedures.

C's private physician refers him to the hospital's outpatient diagnostic facilities for a specific diagnostic procedure. The procedure is administered by a hospital-based practitioner affiliated with the hospital. The availability of these diagnostic procedure is an integral part of the services offered by the hospital. C is a 'patient' of the hospital.

Situation 4-A person refilling a prescription written during the course of his treatment as a patient of the hospital.

D was formerly a patient of the hospital. During his course of treatment the attending staff physician gave D a prescription. D filled the prescription at the hospital pharmacy, which filed and retained it. After formal discharge as a patient, he finds it convenient to return to the hospital pharmacy to obtain a refill of that prescription. Since the prescription was written in the course of the hospital-patient relationship, D is a 'patient' of the hospital.

Situation 5-A person receiving medical services as part of a hospital administered home care program.

E receives medical services in his residence. The services are rendered by, and under the supervision of, the professional staff of the hospital as an extension of its inpatient and outpatient care. E is a 'patient' of the hospital.

Situation 6-A person receiving medical care and services in a hospital-affiliated extended care facility.

F is a patient in an extended care facility qualified to participate in Medicare and other government financed programs. The facility is affiliated with the hospital which, by agreement, is responsible for certain of its professional activities, especially those necessary to qualify the facility for participating in the Medicare program. While a patient in the facility, F is under the medical supervision of a member of the hospital's medical staff and thus is a 'patient' of the hospital.

Accordingly, sales of pharmaceutical supplies to the 'patients' in each of the situations described do not constitute unrelated trade or business of the hospital within the meaning of section 513 of the Code.

See Revenue Rulings 68-374 and 68-375, pages 242 and 245 of this Bulletin, for other situations involving sales of pharmaceutical supplies by pharmacies operated by hospitals.