



## MULTISTATE INDIRECT TAX

# Iowa Court of Appeals denies healthcare sales and use tax flow-through exemption Tax Alert

## Overview

In [\*Health Enterprises of Iowa v. Iowa Department of Revenue\*](#), the Iowa Court of Appeals (“Court of Appeals”) affirmed the lower court’s decision holding that Iowa Code section 423.3(27) unambiguously requires a taxpayer to be a “nonprofit hospital licensed pursuant to chapter 135B” to qualify for the sales tax exemption for nonprofit hospitals. The Court of Appeals rejected the argument that the taxpayer, Health Enterprises, can claim a flow-through exemption based on the eligibility of its members.

This Tax Alert summarizes this recent Iowa decision.

## Iowa’s sales and use tax exemption for nonprofit hospitals

Iowa allows a sales and use tax exemption for goods and services sold “to a nonprofit hospital licensed pursuant to chapter 135B” under Iowa Code section 423.3(27). An entity qualifies for the exemption if two conditions are met: “(1) the tax-exempt goods or services must be sold to a nonprofit hospital licensed pursuant to chapter 135B, and (2) the tax-exempt goods or services must be used in the operation of the hospital.”

## Court of Appeals decision

Iowa chapter 135B.1 defines a hospital as “a place which is devoted primarily to the maintenance and operation of facilities for the diagnosis, treatment or care over a period exceeding twenty-four hours of two or more nonrelated individuals suffering from illness, injury, or deformity, or a place which is devoted primarily to the rendering over a period exceeding twenty-four hours of obstetrical or other medical nursing care for two or more nonrelated individuals, or any institution, place, building or agency in which any accommodation is primarily maintained, furnished or offered for the care over a period exceeding twenty-four hours of two or more nonrelated aged or infirm persons requiring or receiving chronic or convalescent care...”

Health Enterprises is an Iowa chapter 504 nonprofit corporation that provides purchasing activities and other shared services to Iowa hospitals. Health Enterprises does not meet the above definition of “hospital” under chapter 135B. However, Health Enterprises argued they should qualify as a “nonprofit hospital licensed pursuant to chapter 135B” because they purchase goods and services for their nonprofit hospital members. Health Enterprises claimed Iowa’s sales tax exemption should “flow-through” from such member entities and they should be entitled to a refund for sales and use tax paid on certain goods and services furnished to chapter 135B-licensed nonprofit hospitals within their group.

The Court of Appeals ruled that the exemption outlined in Iowa Code section 423.3(27) does not flow through to healthcare entity members who are not themselves a nonprofit hospital licensed pursuant to chapter 135B. The decision stated that the statute is unambiguous and there is no indication that “an entity that is not, itself, a nonprofit hospital licensed under chapter 135B is eligible for the exemption in section 423.3(27).” The Court of Appeals emphasized that tax exemptions must be strictly construed and that the flow-through exemption theory is nowhere in the statute nor between the statute's lines. Even though Health Enterprises’ members are qualified nonprofit hospitals, the taxpayer is not a nonprofit hospital licensed under Iowa Code chapter 135B, and the sales and use tax refund claim was rightfully denied.

## Impact of decision

Based on this final decision, an entity centrally purchasing goods and services for its nonprofit hospitals licensed under Iowa Code chapter 135B cannot itself take advantage of the nonprofit hospital sales and use tax exemption under Iowa Code section 423.3(27). Non-qualifying entities will be required to collect and remit sales and use tax on goods and services purchased or furnished, even when purchased or furnished within a member group that includes qualified non-profit hospitals.

## Get in touch

[Traci Cull](#)

[Robyn Staros](#)



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30 Rockefeller Plaza  
New York, NY 10112-0015  
United States

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