

# IOWA SALES TAX EXEMPTION CERTIFICATES

*An Iowa Sales Tax Exemption Certificate is required when normally taxable items or services are sold tax free. Usually, these are items for resale or for use in processing, but there are also other reasons for exemption. It is important that the seller knows when to accept an exemption certificate. If audited, the seller will use exemption certificates to support tax exempt sales. A valid certificate taken in good faith will pass the tax burden for unreported sales tax from the seller directly to the purchaser.*

## **Sales tax 'exemption numbers' are not issued in Iowa**

The Iowa Department of Revenue does *not* issue sales tax "exemption numbers" which make purchases by individuals or organizations exempt from sales tax. The purchaser's sales tax permit number is *not* an "exemption number."

## **The purchaser must complete a Sales Tax Exemption Certificate**

When normally taxable sales are made free of sales or use tax, the seller must require the purchaser to complete and sign a Sales Tax Exemption Certificate. This certificate is a proper record of the tax-exempt transaction and must be retained by the seller for at least five years. It identifies the purchaser, the purchaser's business, the items being purchased and the reason for exemption. The purchaser must sign and date the certificate. The purchaser's sales tax permit number must be recorded on the certificate if the purchaser is a retailer.

Keep all exemption certificates on file for a minimum of five years.

## **A 'blanket' exemption certificate is accepted in some cases**

If the purchaser repeatedly makes tax exempt purchases of similar items or services from the same seller, the seller may accept a blanket exemption certificate. The seller can keep this single certificate on file to cover repeat purchases. The seller must periodically verify that the information on the blanket exemption certificate is accurate and complete. Keep all blanket exemption certificates on file for a minimum of five years.

## **The exemption certificate must be accepted 'in good faith'**

An exemption certificate must be thoroughly completed by the purchaser and accepted in good faith by the seller to be regarded as valid. To satisfy the "good faith" requirement, the seller must reasonably believe that the items or services being purchased will be used in the exempt manner claimed by the purchaser.

For example, a prudent businessperson would accept an exemption certificate from a florist purchasing decorative vases for resale. However, if the same florist attempted to buy shoes free of tax, the exemption certificate would not pass the good faith test.

In an audit situation, the department will not recognize an exemption certificate which fails to meet the "good faith" test. The seller may be held responsible for any sales tax due from such transactions.

The seller must question the purchaser's claim of exemption when evidence or circumstances indicate that the items or services purchased will not be used in an exempt manner. If the seller remains

unconvinced that the sale is exempt, then the sale should be taxed. *The seller is not required to make a tax-exempt sale.*

This good faith test is also applied, of course, in the case of a blanket exemption certificate.

### **How to determine if a transaction is exempt**

Most of the reasons which make a transaction exempt from Iowa sales tax are listed on the exemption certificate itself. The instructions on the back of the certificate further clarify these reasons.

Below are the exemption explanations found on the back of the exemption certificate.

#### **Exemptions:**

**Resale:** Any person in the business of selling who is purchasing items to resell may claim this exemption. The purchaser can be acting as either a retailer or wholesaler and may not be required to have a sales tax permit. Retailers who do have a sales tax permit number must enter it in the space provided.

**Processing:** Exempt purchases for processing include tangible personal property which by means of fabrication, compounding, manufacturing or germination becomes an integral part of other tangible personal property ultimately sold at retail; chemicals, solvents, sorbents or reagents used, consumed, dissipated or depleted in processing personal property intended to be sold ultimately at retail; fuel used to create heat, power or steam for processing or used to generate electric current; and chemicals used in the production of free newspapers and shoppers.

**Leasing:** Exemption is applicable only to property leased where the lessor is in the business of leasing, the lease is for more than five months, and the lease or rental receipts are subject to Iowa sales tax.

**Qualifying Farm Machinery/Equipment:** The farm machinery or equipment must be directly and primarily used in agricultural production; and must be:

- | a self-propelled implement such as a tractor
- | a grain dryer (heater and blower only)
- | an implement customarily drawn or attached to a self-propelled implement in the performance of its function, such a plow
- | non self-propelled equipment that does not become a part of real property used in dairy and livestock operations
- | an essential replacement part for any of the above

**Qualifying Industrial Machinery/Equipment/Computers:** This machinery or equipment must be:

- | used by a manufacturer
- | directly and primarily used in processing tangible personal property or certain other research activities
- | a replacement part for the above

**Direct Pay:** Businesses and individuals who have a tax liability of more than \$4,000 in state sales and use taxes in a semi-monthly period can pay their taxes directly to the Department rather than to the seller. They **must** enter their Direct Pay permit number in the space provided.

**Private Nonprofit Educational Institutions:** Purchases made by private nonprofit educational institutions used for educational purposes are exempt.

NOT EXEMPT from sales tax are purchases by most other private nonprofit organizations such as churches, fraternal organizations, etc., for use by those organizations.

**Construction contractors are not always exempt from paying tax**

*Contractor-retailers* who make purchases for resale may do so without paying tax. They must, of course, complete an exemption certificate.

*Contractors* who purchase building materials and supplies for construction projects must pay tax on their purchases.

**Most nonprofit organizations must pay sales and use taxes**

Common examples of nonprofit organizations include churches, church groups, Boy Scouts, Girl Scouts, Jaycees, Kiwanis, American Legion, 4-H, booster clubs and other similar groups. These groups must pay Iowa sales or use tax on purchases of taxable items and services for their own use just like any other customer. While these groups may hold Iowa sales tax permits for taxable sales, having a sales tax permit does not make them exempt from paying tax on purchases for their own use.

**A few nonprofit entities are exempt from paying sales tax**

The Iowa Code *does* exempt certain specific nonprofit entities from paying sales tax on purchases. The most common of these are government agencies and subdivisions, including schools. (For a complete list of entities which are not required to pay Iowa sales tax, request our "Iowa Tax Guide for Nonprofit Entities.") These exempt entities *must* pay for their purchases with a check or voucher drawn on the entity's account or with a credit card set up the same way.

Even when the purchaser is a government agency, school or other exempt entity, the seller should require the purchaser to complete and sign a Sales Tax Exemption Certificate. If the purchaser repeatedly makes tax-exempt purchases of similar items, the seller may accept a blanket exemption certificate.

**Produce your own forms**

The department will recognize substitute Sales Tax Exemption Certificate forms, provided they meet certain requirements. In order to be valid, a substitute form must include: the seller's name, the purchaser's name and address, the purchaser's nature of business (wholesaler, retailer, manufacturer, lessor, other), reason for exemption (resale, processing, other), general description of the products purchased and the purchaser's Iowa sales tax or I.D. registration number (if the purchaser is a retailer). The purchaser must sign and date the certificate.