

March 31, 1959.
Passed on File.

Senate File 506
By COMMITTEE ON TAX REVISION.

Passed Senate, Date..... Passed House, Date.....
Vote: Ayes..... Nays..... Vote: Ayes..... Nays.....
Approved.....

A BILL FOR

An Act relating to the formula by which income of corporations is to be apportioned between the state of Iowa and other states for purposes of the Iowa income tax on corporations.

Be It Enacted by the General Assembly of the State of Iowa:

1 Section 1. Section four hundred twenty-two point thirty-three
2 (422.33), Code 1958, is hereby repealed and the following enacted
3 in lieu thereof:

4 "A tax is hereby imposed upon each corporation organized under
5 the laws of this state, and upon every foreign corporation
6 engaged in income producing activities in this state, annually
7 in an amount equivalent to two percent of the net income received
8 by such corporation during the income year.

9 1. If the income producing activities of the corporation are
10 carried on entirely within the state, the tax shall be imposed on
11 the entire net income, but if such income producing activities
12 are carried on partly within and partly without the state, the
13 tax shall be imposed only on the portion of the net income
14 reasonably attributable to the state, said net income
15 attributable to the state to be determined as follows:

16 a. Interest, dividends, rents, and royalties (less stated
17 expenses) received in connection with income producing activities
18 in the state, shall be allocated to the state, and where received
19 in connection with income producing activities outside the state
20 shall be allocated outside the state.

21 b. Net income of the above class having been separately
22 allocated and deducted as above provided, the remainder of the
23 net income of the taxpayer shall be allocated and apportioned as
24 follows:

25 Where income is derived from income producing activities other
26 than the manufacture or sale of tangible personal property or
27 compensation for performance of labor or personal services, such
28 income shall be specifically allocated or equitably apportioned
29 within and without the state under rules and regulations of the
30 commission.

31 Where income is derived from the manufacture or sale of
32 tangible personal property, the part thereof attributable to
33 income producing activities within the state shall be allocated
34 to Iowa on the basis of the percentage computed by taking the
35 arithmetical average of the following three percentages:

36 (1). The percentage which the sales made in Iowa is of total
37 sales wherever made. Sales made in Iowa include sales made
38 through, from, or by offices, agencies, branches, stores or
39 personal solicitation of salesmen or representatives in Iowa,
40 whether or not such salesmen or representatives are residents of
41 Iowa, and whether or not such sales are consummated by delivery
42 of the goods sold in interstate commerce.

43 (2). The percentage which the total tangible property, real,
44 personal, and mixed, owned or used by the taxpayer in this state
45 in connection with such income producing activities, is of the
46 total tangible property, real, personal, or mixed, wherever
47 located, owned, or used by the taxpayer in connection with such
48 income producing activities; and,

49 (3). The percentage which the taxpayer's total payrolls paid

50 or incurred in this state or paid in respect to labor performed
51 in this state in connection with such income producing activities
52 is of the taxpayer's total payrolls paid or incurred in
53 connection with such income producing activities.

54 (4). In computing the percentages under subparagraphs
55 one (1), two (2) and three (3) above the valuation of transient
56 property, such as motor vehicles, shall be apportioned in a
57 manner to reflect the use of such property within and without the
58 state of Iowa. The valuation of tangible property, other than
59 inventories, shall be its depreciated tax cost for income tax
60 purposes at the end of the tax year, except that if such
61 valuation does not fairly reflect the total tangible property
62 owned or used by the taxpayer in this state during such tax year,
63 such valuation shall be the average valuation of such property so
64 owned or used during the tax year to be determined on the basis
65 of sound accounting practices. All inventories shall be valued
66 at total book cost at the end of the tax year, except that if
67 such book cost does not fairly reflect the total inventory owned
68 or used by the taxpayer during the tax year, such valuation shall
69 be the average valuation of such property so owned or used during
70 the tax year to be determined on the basis of sound accounting
71 practices. For corporations occupying rented properties or using
72 leased equipment, such property shall be valued at eight (8)
73 times the annual net rental payments. For purposes of this
74 computation, payrolls shall include wages, salaries, commissions,
75 bonuses, and all remuneration paid as compensation for employees'
76 personal services and shall be considered payrolls paid or
77 incurred in this state, or paid in respect to labor performed in
78 this state, if the duties of the employee normally require said

79 employee to spend one-half or more of his working time in Iowa,
80 without regard to the legal residence of the employee.

81 For corporations engaged in the sale of tangible personal
82 property within this state but not engaged in the manufacture of
83 tangible personal property within this state and which are
84 neither domestic corporations of this state or domiciled in this
85 state, the income remaining, after the deductions provided for in
86 paragraphs a. and b. of this subsection, shall be allocated to
87 Iowa in that proportion which the gross sales made within the
88 state bear to the total gross sales. The words 'gross sales made
89 within the state' shall include all sales to be included in the
90 Iowa portion of total sales under the provisions of subparagraph
91 (1) of paragraph b. of this subsection.

92 Income derived from compensation for labor or personal
93 services or from income producing activities consisting
94 principally of the performance of personal or professional
95 services, shall be allocated to Iowa in that proportion which the
96 gross receipts made within the state bear to the total gross
97 receipts.

98 For the purpose of this section, the word 'sale' shall include
99 exchange, and the word 'manufacture' shall include the extraction
100 and recovery of natural resources and all processes of
101 fabricating and curing. The words 'tangible personal property'
102 shall be taken to mean corporeal personal property, such as
103 machinery, tools, implements, goods, wares, and merchandise, and
104 shall not be taken to mean money deposits in banks, shares of
105 stock, bonds, notes, credits, or evidence of an interest in
106 property and evidences of debt.

107 2. If any taxpayer believes that the method of allocation and

108 apportionment hereinbefore prescribed, as administered by the
109 commission and applied to his income producing activities has
110 operated or will so operate as to subject him to taxation on a
111 greater portion of his net income than is reasonably attributable
112 to income producing activities within the state, he shall be
113 entitled to file with the commission a statement of his
114 objections and of such alternative method of allocation and
115 apportionment as he believes to be proper under the circumstances
116 with such detail and proof and within such time as the commission
117 may reasonably prescribe; and if the commission shall conclude
118 that the method of allocation and apportionment theretofore
119 employed is in fact inapplicable and inequitable it shall
120 redetermine the taxable income by such other method of allocation
121 and apportionment as seems best calculated to assign to the state
122 for taxation the portion of the income reasonably attributable to
123 income producing activities within the state.

124 3. If it shall appear to the tax commission that any
125 allocation percentage determined as hereinabove provided does not
126 properly reflect the income producing activities of a taxpayer
127 within the state, the tax commission shall be authorized in its
128 discretion, in case of the corporation allocation percentage, to
129 adjust it by (a) excluding one or more of the factors therein,
130 (b) including one or more other factors, or (c) any other similar
131 or different method calculated to effect a fair and proper
132 allocation of income reasonably attributable to the state. Upon
133 such action by the tax commission the taxpayer will be informed
134 in writing of the method to be used to allocate and apportion the
135 income attributable to the state."

1 Sec. 2. Section four hundred twenty-two point forty (422.40),

- 2 Code 1958, is hereby amended by striking from lines five (5) and
 3 six (6) of subsection one (1) the words, "doing business in this
 4 state for profit" and by inserting in lieu thereof the words,
 5 "engaged in income producing activities in this state".

EXPLANATION OF SENATE FILE 506

ADOPTION OF THE THREE-FACTOR ALLOCATION FORMULA

It is proposed that the present method of allocation (using only the sales factor) be replaced by a 3-factor formula using sales, property and payroll as elements of the formula. Net income attributable to Iowa would then be computed as follows:

1. The percentage of Iowa sales to total sales would be computed.
2. The percentage of real and personal property in Iowa to total property wherever located would be computed. In this computation rented property would be included and valued at eight times the annual rent.
3. The percentage of the payroll paid to Iowa employees to total payroll would be computed.
4. The average of these three percentages would then be computed. This average would be the percentage of total net income allocated to Iowa for taxation.

In cases where either the tax commission or taxpayer was able to demonstrate that the formula would not result in an allocation which fairly reflected the taxpayer's Iowa income, the tax commission would be authorized to require or permit the use of a different method to achieve a fair result.

Examples of How the Amendment Would Work

The following examples show how the present law and the proposed amendment would operate for several fictitious example corporations, each having an income after federal taxes of \$100,000.

Example 1: Retailer doing business exclusively in Iowa

Percent of sales in Iowa.....	100%
Percent property in Iowa.....	100%
Percent of payroll in Iowa.....	100%
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Average	100%
Income allocated to Iowa—present law.....	\$100,000
Tax under present law.....	\$ 2,000
Income allocated by 3-factor formula.....	\$100,000
Tax using 3-factor formula.....	\$ 2,000

Example 2: Iowa manufacturer selling on nation-wide market

Percent of sales in Iowa.....	10%
Percent of employees in Iowa.....	90%
Percent of property in Iowa.....	95%
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Average	65%
Income allocated to Iowa—present law.....	\$ 10,000
Tax under present law.....	\$ 200
Income allocated by 3-factor formula.....	\$ 65,000
Tax using 3-factor formula.....	\$ 1,300

Example 3: Iowa wholesaler selling in several state areas

Percent of sales in Iowa.....	40%
Payroll in Iowa.....	100%
Property in Iowa.....	100%
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Average	80%
Income allocated to Iowa—present law.....	\$ 40,000
Tax under present law.....	\$ 800
Income allocated by 3-factor formula.....	\$ 80,000
Tax using 3-factor formula.....	\$ 1,600

Example 4: Out-of-state wholesaler or manufacturer selling on the national market

Percent of sales in Iowa.....	10%
Income allocated to Iowa—present law.....	\$ 10,000
Tax under present law.....	\$ 200
Income allocated to Iowa—under this Act.....	\$ 10,000
Tax using this Act.....	\$ 200