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FILED APR 24 1989

Ways & Means

SENATE FILE 537

BY COMMITTEE ON

WAYS AND MEANS

Passed Senate, Date 4-26-89 (p. 1696) Passed House, Date 5-3-89 (p. 2393)

Vote: Ayes 37 Nays 10 Vote: Ayes 93 Nays 6

Approved May 31, 1989

A BILL FOR

3933

1 An Act relating to the standard deduction for state individual  
2 income tax purposes, limiting the deduction for net capital  
3 gain to the transfer of certain capital assets, providing an  
4 earned income tax credit, and providing retroactive  
5 applicability and effective dates.

6 BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF IOWA:

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SF 537

3924-1 Section 1. Section 422.4, subsection 17, paragraph a, Code  
2 1989, is amended to read as follows:

3 a. "Annual inflation factor" means an index, expressed as  
4 a percentage, determined by the department by October 15 of  
5 the calendar year preceding the calendar year for which the  
6 factor is determined, which reflects the purchasing power of  
7 the dollar as a result of inflation during the fiscal year  
8 ending in the calendar year preceding the calendar year for  
9 which the factor is determined. In determining the annual  
10 inflation factor, the department shall use the annual percent  
11 change, but not less than zero percent, in the implicit price  
12 deflator for the gross national product computed for the  
13 second quarter of the calendar year by the bureau of economic  
14 analysis of the United States department of commerce and shall

3930-15 add ~~one-half~~ one-fourth of that percent change to one hundred  
16 percent. The annual inflation factor and the cumulative  
17 inflation factor shall each be expressed as a percentage  
18 rounded to the nearest one-tenth of one percent. The annual  
19 inflation factor shall not be less than one hundred percent.

20 Sec. 2. Section 422.4, subsection 17, paragraph c, Code  
21 1989, is amended to read as follows:

22 c. The annual inflation factor for the 1988 calendar year  
23 is one hundred percent. The annual inflation factor for the  
24 1990 calendar year is one hundred percent, notwithstanding the  
25 computation under paragraph "a".

3929-26 Sec. 3. Section 422.4, Code 1989, is amended by adding the  
27 following new subsection:

28 NEW SUBSECTION. 18. a. "Annual standard deduction  
29 factor" means an index, expressed as a percentage, determined  
30 by the department by October 15 of the calendar year preceding  
31 the calendar year for which the factor is determined, which  
32 reflects the purchasing power of the dollar as a result of  
33 inflation during the fiscal year ending in the calendar year  
34 preceding the calendar year for which the factor is  
35 determined. In determining the annual standard deduction .

1 factor, the department shall use the annual percent change,  
2 but not less than zero percent, in the implicit price deflator  
3 for the gross national product computed for the second quarter  
4 of the calendar year by the bureau of economic analysis of the  
5 United States department of commerce and shall add the total  
6 percent change to one hundred percent. The annual standard  
7 deduction factor and the cumulative standard deduction factor  
8 shall each be expressed as a percentage rounded to the nearest  
9 one-tenth of one percent. The annual standard deduction  
10 factor shall not be less than one hundred percent.

11 b. "Cumulative standard deduction factor" means the  
12 product of the annual standard deduction factor for the 1989  
13 calendar year and all annual standard deduction factors for  
14 subsequent calendar years as determined pursuant to this  
15 subsection. The cumulative standard deduction factor applies  
16 to all tax years beginning on or after January 1 of the  
17 calendar year for which the latest annual standard deduction  
18 factor has been determined.

19 c. The annual standard deduction factor for the 1989  
20 calendar year is one hundred percent.

21 d. Notwithstanding the computation of the annual standard  
22 deduction factor under paragraph "a", the annual standard  
23 deduction factor is one hundred percent for any calendar year  
24 beginning after December 31, 1990, in which the unobligated  
25 state general fund balance on June 30, as certified by the  
26 director of revenue and finance by October 10, is less than  
27 sixty million dollars.

2431, 3133

28 Sec. 4. Section 422.9, subsection 6, unnumbered paragraph  
29 1, Code 1989, is amended by striking the unnumbered paragraph  
30 and inserting in lieu thereof the following:

31 The taxpayer may recompute the taxpayer's income tax  
32 liability for the tax year by subtracting from the taxpayer's  
33 taxable income, as computed without regard to this subsection,  
34 sixty percent of the net capital gain from the sale of the  
35 following:

1 a. Net capital gain from the sale of real property used in  
2 a business, in which the taxpayer materially participated, as  
3 defined in section 469(h) of the Internal Revenue Code, and  
4 which has been held for a minimum of ten years, or from the  
5 sale of a business in which the taxpayer was employed or in  
6 which the taxpayer materially participated, as defined in  
7 section 469(h) of the Internal Revenue Code, and which has  
8 been held for a minimum of ten years. The sale of a business  
9 means the sale of all or substantially all of the tangible  
10 personal property or services of the business.

11 b. Net capital gain from the sale of cattle or horses held  
12 by the taxpayer for breeding, draft, dairy, or sporting  
13 purposes for a period of twenty-four months or more from the  
14 date of acquisition; but only if the taxpayer received more  
15 than one-half of the taxpayer's gross income from farming or  
16 ranching operations in this state during the tax year.

17 c. Net capital gain from the sale of breeding livestock,  
18 other than cattle or horses, if the livestock is held by the  
19 taxpayer for a period of twelve months or more from the date  
20 of acquisition; but only if the taxpayer received more than  
21 one-half of the taxpayer's gross income from farming or  
22 ranching operations in this state during the tax year.

23 The net long-term capital gain of paragraphs "a", "b", and  
24 "c" together shall not exceed seventeen thousand five hundred  
25 dollars for the tax year. Married taxpayers who elect  
26 separate filing on a combined return for state tax purposes  
27 are treated as one taxpayer and the amount of net capital gain  
28 to be used to determine the total amount to be subtracted by  
29 them shall not exceed seventeen thousand five hundred dollars  
30 in the aggregate. Married taxpayers who file jointly or  
31 separately on a combined return shall prorate the seventeen  
32 thousand five hundred dollar limitation between them based on  
33 the ratio of each spouse's net capital gain to the total net  
34 capital gain of both spouses. In the case of married  
35 taxpayers filing separate returns, the amount of net capital

1 gain to be used to determine the amount to be subtracted by  
 2 each spouse shall not exceed eight thousand seven hundred  
 3 fifty dollars.

4 Sec. 5. Section 422.9, subsection 5, unnumbered paragraph  
 5 4, Code 1989, is amended to read as follows:

6 For the tax year the total amount of refund claims that  
 7 shall be paid shall not exceed eight million dollars. If the  
 8 total amount of the claims for refund does exceed that amount,  
 9 each claim for refund shall be paid on a pro rata basis so  
 10 that the total amount paid for the tax year does not exceed  
 11 eight million dollars. In the case where refund claims are  
 12 not paid in full, the amount of the refund to which the  
 13 taxpayer is entitled under this subsection is the pro rata  
 14 amount that was paid and the taxpayer is not entitled to a  
 15 refund for the unpaid portion and is not entitled to carry  
 16 that amount forward or backward to another tax year.

17 Taxpayers shall not use refunds as estimated payments for the  
 18 succeeding tax year. ~~Taxpayers whose tax years begin on~~  
 19 ~~January 1 must file their refund claims by October 31, 1988,~~  
 20 ~~to be eligible for refunds.--Taxpayers whose tax years begin~~  
 21 ~~on a date in 1987 other than January 1 must file their refund~~  
 22 ~~claims by the end of the sixth month following the end of~~  
 23 ~~their tax years.--The department shall determine on February~~  
 24 ~~15, 1989, if the total amount of claims for refund exceeds~~  
 25 ~~eight million dollars for the tax year.--Notwithstanding any~~  
 26 ~~other provision, interest shall not be due on any refund~~  
 27 ~~claims that are paid by February 28, 1989.--If the claims is~~  
 28 ~~not payable on February 28, 1989, because the taxpayer has~~  
 29 ~~filed a year later, then the amount of the claim allowed shall~~  
 30 ~~be in the same ratio to refund claims available on February 28,~~  
 31 ~~1989.--These claims shall be funded by moneys appropriated for~~  
 32 ~~payment of refunds of individual income tax. The deadline for~~  
 33 ~~filing a claim for a refund for calendar year taxpayers whose~~  
 34 ~~tax years begin on January 1 is October 31 following the~~  
 35 ~~calendar year. The department shall determine on February 1~~

1 following the October 31 deadline, if the total amount of  
2 claims for refund exceeds eight million dollars for the tax  
3 year. Notwithstanding any other provision, interest shall not  
4 be due on any refund claims that are paid by February 28  
5 following the October 31 deadline. Taxpayers whose tax years  
6 begin on a date other than January 1 must file their refund  
7 claims by the end of the sixth month following the end of  
8 their tax years. If the claim is not payable on February 28  
9 following the October 31 deadline of calendar year taxpayers,  
10 because the taxpayer is a fiscal year filer, then the amount  
11 of the claim allowed shall be the same ratio as refund claims  
12 available February 1 following the October 31 deadline. These  
13 claims shall be funded by moneys appropriated for payment of  
14 refunds of individual income tax.

35433  
15 Sec. 6. NEW SECTION. 422.12B EARNED INCOME TAX CREDIT.

16 1. The taxes imposed under this division, less credits  
17 allowed under sections 422.10 through 422.12, shall be reduced  
18 by an earned income credit equal to ten percent of the federal  
19 earned income credit received by the taxpayer under section  
20 32(b) of the Internal Revenue Code. Any credit in excess of  
21 the tax liability is nonrefundable.

22 2. Married taxpayers electing to file separate returns or  
23 filing separately on a combined return may avail themselves of  
24 the earned income credit by allocating the earned income  
25 credit to each spouse in the proportion that each spouse's  
26 respective earned income bears to the total combined earned  
27 income. Taxpayers affected by the allocation provisions of  
28 section 422.8 shall be permitted a deduction for the credit  
29 only in the amount fairly and equitably allocable to Iowa  
30 under rules prescribed by the director.

31 Sec. 7. Section 422.21, Code 1989, is amended by adding  
32 the following new unnumbered paragraph:

33 NEW UNNUMBERED PARAGRAPH. The director shall determine for  
34 the 1990 and each subsequent calendar year the annual and  
35 cumulative standard deduction factors for each calendar year

1 to be applied to tax years beginning on or after January 1 of  
2 that calendar year. The director shall compute the new  
3 standard deduction dollar amounts as specified in section  
4 422.9, subsection 1, by the latest cumulative standard  
5 deduction factor and round off the result to the nearest ten  
6 dollars. The annual and cumulative standard deduction factors  
7 determined by the director are not rules as defined in section  
8 17A.2, subsection 7.

3429- 9 Sec. 8. Section 1 of this Act takes effect January 1,  
10 1991, for tax years beginning on or after that date.

11 Sec. 9. Sections 2 and 3 of this Act take effect January  
12 1, 1990, for tax years beginning on or after that date.

3430, 3435-13 Sec. 10. Sections 4, 5, and 6 of this Act apply  
14 retroactively to January 1, 1989, for tax years beginning on  
15 or after that date.

16 EXPLANATION

17 The bill requires the director of revenue and finance to  
18 annually index the standard deduction for individual income  
19 tax purposes beginning with the 1990 tax years. Current law  
20 only indexes the income tax brackets and certain federal  
21 pension deductions.

22 The bill also limits the present capital gain deduction  
23 refund claim to individuals whose net capital gains are from  
24 certain business assets.

25 The bill also provides a state earned income tax credit for  
26 individuals. The credit is equal to ten percent of the  
27 federal earned income credit. The credit is nonrefundable.

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## SENATE FILE 537

S-3933

1 Amend Senate File 537 as follows:

- A 2 1. Page 2, by inserting after line 27, the  
3 following:  
4 "Sec. 100. Section 422.5, subsection 1, paragraph  
5 k, subparagraph (1), Code 1989, is amended to read as  
6 follows:  
7 (1) Add items of tax preference included in  
8 federal alternative minimum taxable income under  
9 section 57, except subsections (a)(1), (a)(2), and  
10 (a)(5), of the Internal Revenue Code, make the  
11 adjustments included in federal alternative minimum  
12 taxable income under section 56, except subsections  
13 (a)(4), (b)(1)(C)(iii), and (d), of the Internal  
14 Revenue Code, and add losses as required by section 58  
15 of the Internal Revenue Code, and add the capital gain  
16 deduction subtracted from net income in subsection 19  
17 of section 422.7. In the case of an estate or trust,  
18 the items of tax preference, adjustments, and losses  
19 shall be apportioned between the estate or trust and  
20 the beneficiaries in accordance with rules prescribed  
21 by the director."  
22 2. Page 2, by inserting after line 27, the  
23 following:  
24 "Sec. 101. Section 422.7, Code 1989, is amended by  
25 adding the following new subsection:  
26 NEW SUBSECTION. 19. Subtract sixty percent of the  
27 net capital gain as computed in section 1202 of the  
28 Internal Revenue Code in effect for tax years  
29 beginning in the 1986 calendar year. For purposes of  
30 determining the amount to be subtracted, the net  
31 capital gain shall not exceed one thousand eight  
32 hundred dollars. Married taxpayers who elect separate  
33 filing on a combined return for state tax purposes are  
34 treated as one taxpayer and the amount of net capital  
35 gain to be used to determine the total amount to be  
36 subtracted by them shall not exceed one thousand eight  
37 hundred dollars in the aggregate. Married taxpayers  
38 who file jointly or separately on a combined return  
39 shall prorate the one thousand eight hundred dollar  
40 limitation between them based on the ratio of each  
41 spouse's net capital gain to the total net capital  
42 gain of both spouses. In the case of married  
43 taxpayers filing separate returns, the amount of net  
44 capital gain to be used to determine the amount to be  
45 subtracted by each spouse shall not exceed nine  
46 hundred dollars. Any income or loss resulting from  
47 the forfeiture, transfer, or sale or exchange  
48 described in section 422.7, subsection 17, shall not  
49 be used in computing net capital gain for purposes of  
50 this subsection."

S-3933

Page 2

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A 1 3. By striking page 2, line 28 through page 5,  
 2 line 14 and inserting the following:  
 3 "Sec. 102. Section 422.9, subsection 6, Code 1989,  
 4 is amended by striking the subsection."

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B 5 4. Page 5, by inserting before line 15 the  
 6 following:  
 7 "Sec. 103. Section 422.12, subsection 2,  
 8 unnumbered paragraph 1, Code 1989, is amended to read  
 9 as follows:  
 10 A child and dependent care credit equal to forty-  
 11 ~~five~~ fifty-five percent of the federal child and  
 12 dependent care credit provided in section 21 of the  
 13 Internal Revenue Code."

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14 5. Page 5, by striking lines 15 through 30.  
 A 15 6. Page 6, line 13, by striking the figures and  
 16 word "4, 5, and 6" and inserting the following: "100,  
 17 101, 102, and 103".

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B 18 7. Title page, lines 3 and 4, by striking the  
 19 words "providing an earned income" and inserting the  
 20 following: "increasing the child and dependent care".

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21 8. By renumbering as necessary.

|                      |                 |
|----------------------|-----------------|
| By CALVIN O. HULTMAN | JACK W. HESTER  |
| RICHARD F. DRAKE     | JOHN W. JENSEN  |
| LINN FUHRMAN         | JULIA GENTLEMAN |
| NORM GOODWIN         | WILMER RENSINK  |
| JIM LIND             | MARK R. HAGERLA |
| PAUL PATE            | DALE L. TIEDEN  |
| JACK RIFE            | RAY TAYLOR      |
| RICHARD VANDE HOEF   | MAGGIE TINSMAN  |
| JOHN SOORHOLTZ       |                 |

S-3933 FILED APRIL 26, 1989  
 DIVISION A-LOST, DIVISION B-LOST

*4-26-89 (p-11/110)*

## SENATE FILE 537

S-3931

1 Amend Senate File 537 as follows:

2 1. Page 2, by inserting after line 27 the  
3 following:

4 "Sec. 30. Section 422.5, Code 1989, is amended by  
5 adding the following new subsection:

6 NEW SUBSECTION. 10. In the case of income derived  
7 from the sale or exchange of livestock in excess of  
8 the number the taxpayer would sell if the taxpayer  
9 followed the taxpayer's usual business practices, a  
10 taxpayer may elect to spread the income equally over  
11 the four tax years following the tax year in which  
12 such sale or exchange occurs if the taxpayer  
13 establishes that, under the taxpayer's usual business  
14 practices, the sale or exchange would not have  
15 occurred in the taxable year in which it occurred if  
16 it were not for drought conditions or other act of  
17 God. This subsection shall apply only to a taxpayer  
18 whose principal trade or business is farming, within  
19 the meaning of section 6420(c)(3), of the Internal  
20 Revenue Code."

21 2. Page 3, by inserting after line 22 the  
22 following:

23 "d. The gain indicated in income for the tax year  
24 from the sale or exchange of livestock as described in  
25 section 422.5, subsection 10."

26 3. Page 3, lines 23 and 24, by striking the words  
27 "and "c"" and inserting the following: ""c", and  
28 "d"".

29 4. Page 6, line 13, by inserting after the word  
30 "Sections" the following: "30,".

By BERL E. PRIEBE  
KEN SCOTT  
EMIL J. HUSAK  
JOHN A. PETERSON  
EUGENE FRAISE  
JOHN SOORHOLTZ

JACK RIFE  
LEONARD BOSWELL  
DALE L. TIEDEN  
H. KAY HEDGE  
JOHN JENSEN  
RICHARD VANDEHOEF

S-3931 FILED APRIL 26, 1989

ADOPTED

4-26-89 (p. 1185)

## SENATE FILE 537

S-3929

- 1 Amend Senate File 537 as follows:  
 2 1. Page 1, by striking lines 1 through 19.  
 3 2. Page 1, by inserting before line 26, the  
 4 following:  
 5 "Sec. 100. Section 422.4, subsection 17, paragraph  
 6 d, Code 1989, is amended by striking the paragraph."  
 7 3. Page 2, by striking lines 21 through 27.  
 8 4. Page 6, by striking lines 9 and 10.  
 9 5. Page 6, line 13, by striking the words "and 6"  
 10 and inserting the following: "6, and 100".  
 11 6. By renumbering as necessary.

By CALVIN O. HULTMAN  
 RICHARD F. DRAKE  
 JACK W. HESTER  
 LINN FUHRMAN  
 JACK RIFE  
 RICHARD VANDE HOEF  
 JOHN SOORHOLTZ  
 JIM LIND

JOHN JENSEN  
 JULIA GENTLEMAN  
 WILMER RENSINK  
 MARK R. HAGERLA  
 DALE L. TIEDEN  
 RAY TAYLOR  
 MAGGIE TINSMAN

S-3929 FILED APRIL 26, 1989

LOST 4-26-89 (p. 1694)

## SENATE FILE 537

S-3930

- 1 Amend Senate File 537 as follows:  
 2 1. Page 1, line 15, by striking the word "one-  
 3 fourth" and inserting the word "one-third".

By CHARLES BRUNER

S-3930 FILED APRIL 26, 1989

ADOPTED 4-26-89 (p. 1694)

**SENATE FILE 537  
FISCAL NOTE**

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A fiscal note for **SENATE FILE 537 AS AMENDED AND PASSED BY THE SENATE** is hereby submitted pursuant to Joint Rule 17. Data used in developing this fiscal note is available from the Legislative Fiscal Bureau to members of the Legislature upon request.

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Senate File 537 as amended and passed by the Senate requires the Director of Revenue and Finance to annually index the standard deduction for individual income tax purposes beginning with the 1990 tax years. Current law only indexes the income tax brackets and certain federal pension deductions. Additionally, the annual inflation factor (AIF) applied to income brackets and federal pensions is 33% of the AIF instead of 50%. The annual standard deduction factor is not subject to reduction.

The bill also limits the present capital gain deduction refund claim to individuals whose net capital gains are from certain business assets. The bill also provides a state earned income tax credit for individuals. The credit is equal to 10% of the federal earned income credit. The credit is nonrefundable.

Standard deduction indexation: For tax year 1990, the current standard deduction amounts of \$3,030 for married joint filers and \$1,230 for individuals would be indexed by whatever the annual standard deduction factor is determined to be.

For tax year 1991 and subsequent years, standard deduction and income bracket indexation would occur if the ending fund balance of the General Fund was at least \$60.0 million.

**Tax Year 1990 Assumptions**

1. For comparison purposes, estimates for two scenarios are provided: the first scenario assumes current law indexation will not be triggered for Tax Year 1990, the second scenario assumes current law indexation will be triggered for Tax Year 1990.
2. The annual inflation factor and annual standard deduction factor applicable to tax year 1990 is 4.5%, based on information from Data Resources Incorporated.
3. Under current law, if the FY 1989 General Fund ending balance was \$60.0 million, the income brackets in 422.5, Code of Iowa, would be indexed by the product of 50% of the annual inflation factor multiplied by the cumulative inflation factor.
4. Under the proposal, regardless of the General Fund ending balance, income brackets would not be indexed, and the standard deductions would be indexed by the product of the entire amount of the annual standard deduction factor multiplied by the cumulative standard deduction factor.
5. Assuming withholding tables are not changed, these effects would first occur in FY 1991.
6. Civil service annuity exclusions were held constant in this simulation,

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since state tax treatment of government pensions must change.

#### Fiscal Effect, Tax Year 1990, Standard Deduction Indexation

1. Current law basis for comparison assumes bracket indexation will not be triggered for tax year 1990.

The tax model indicates indexing the standard deduction amounts would reduce taxpayer liability by \$3.3 million.

2. Current law basis for comparison assumes indexation will be triggered for tax year 1990

Est. Reduction due to indexation under current law: (\$9.9 million)

Est. Reduction due to indexation under proposal: (\$3.3 million)

#### Tax Year 1991 Assumptions

1. For comparison purposes, estimates for two scenarios are provided: the first scenario assumes current law indexation was not triggered for Tax Year 1990; the second scenario assumes current law indexation was triggered for Tax Year 1990.
2. Indexation will be triggered for Tax Year 1991.
3. The annual inflation factor and annual standard deduction factor applicable to tax year 1991 is 4.2%, based on DRI's April, 1989 report.
4. Under current law, the income brackets in 422.5, Code of Iowa would be indexed by the product of 50% of the annual inflation factor multiplied by the cumulative inflation factor.
5. Under the proposal, income brackets would be increased by the product of 33% of the annual inflation factor multiplied by the cumulative inflation factor, and standard deductions would be increased by the product of the entire amount of the annual standard deduction factor multiplied by the cumulative standard deduction factor.
6. Assuming withholding tables are not changed, this effect would first occur in FY 1992.
7. Civil service annuity exclusions were held constant in this simulation, since state tax treatment of government pensions must change.

#### Fiscal Effect, Tax Year 1991, Bracket and Standard Deduction Indexation

1. Current law basis for comparison assumes bracket indexation was not triggered for tax year 1990.

Est. Reduction due to indexation under current law: (\$9.3 million)

Est. Reduction due to indexation under proposal: (\$9.2 million)

2. Current law basis for comparison assumes bracket indexation was triggered for tax year 1990.

Est. Reduction due to indexation under current law: (\$9.6 million)

Est. Reduction due to indexation under proposal: (\$9.2 million)

Capital Gains Refund Changes: Beginning tax year 1989, only certain types of

-3-

assets would be eligible for the 60% capital gains deduction refund. Generally, the eligible assets must be (a) real property used in a business, or from the sale of a business, in which the taxpayer materially participated, or was employed, and which was held for a minimum of 10 years, or (b) from the sale of livestock by taxpayers deriving more than half of their income from farming or ranching. The \$8.0 million cap on the total amount refunded would continue.

Earned Income tax Credit: A nonrefundable tax credit equivalent to 10% of the taxpayer's federal earned income tax credit is allowed for tax years beginning on or after January 1, 1989. This is estimated by the tax model to reduce taxpayer liability by \$3.2 million. Assuming withholding changes are not made, this effect would first occur in FY 1990.

Sources: Legislative tax model  
Data Resources Incorporated  
Department of Revenue and Finance

(LSB 2721sv, PDD)

FILED APRIL 28, 1989

BY DENNIS PROUTY, FISCAL DIRECTOR

House Ways & Means

DO pass per amend. 4349 (p.2276) 5-1-89

SENATE FILE 537  
BY COMMITTEE ON  
WAYS AND MEANS

(AS AMENDED AND PASSED BY THE SENATE APRIL 26, 1989)  
\_\_\_\_\_ - New Language by the Senate

Passed Senate, Date 5/7/89 (p.2083) Passed House, Date 5-3-89 (p.2393)  
Vote: Ayes 33 Nays 12 Vote: Ayes 93 Nays 6  
Approved May 31, 1989  
Proposed House 5/7/89 (p.2790)  
85-2

A BILL FOR

1 An Act relating to the standard deduction for state individual  
2 income tax purposes, limiting the deduction for net capital  
3 gain to the transfer of certain capital assets, providing an  
4 earned income tax credit, and providing retroactive  
5 applicability and effective dates.

6 BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF IOWA:

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SF 537

4349  
amended

1 Section 1. Section 422.4, subsection 17, paragraph a, Code  
2 1989, is amended to read as follows:

3 a. "Annual inflation factor" means an index, expressed as  
4 a percentage, determined by the department by October 15 of  
5 the calendar year preceding the calendar year for which the  
6 factor is determined, which reflects the purchasing power of  
7 the dollar as a result of inflation during the fiscal year  
8 ending in the calendar year preceding the calendar year for  
9 which the factor is determined. In determining the annual  
10 inflation factor, the department shall use the annual percent  
11 change, but not less than zero percent, in the implicit price  
12 deflator for the gross national product computed for the  
13 second quarter of the calendar year by the bureau of economic  
14 analysis of the United States department of commerce and shall  
15 add ~~one-half~~ one-third of that percent change to one hundred  
16 percent. The annual inflation factor and the cumulative  
17 inflation factor shall each be expressed as a percentage  
18 rounded to the nearest one-tenth of one percent. The annual  
19 inflation factor shall not be less than one hundred percent.

20 Sec. 2. Section 422.4, subsection 17, paragraph c, Code  
21 1989, is amended to read as follows:

22 c. The annual inflation factor for the 1988 calendar year  
23 is one hundred percent. The annual inflation factor for the  
24 1990 calendar year is one hundred percent, notwithstanding the  
25 computation under paragraph "a".

26 Sec. 3. Section 422.4, Code 1989, is amended by adding the  
27 following new subsection:

28 NEW SUBSECTION. 18. a. "Annual standard deduction  
29 factor" means an index, expressed as a percentage, determined  
30 by the department by October 15 of the calendar year preceding  
31 the calendar year for which the factor is determined, which  
32 reflects the purchasing power of the dollar as a result of  
33 inflation during the fiscal year ending in the calendar year  
34 preceding the calendar year for which the factor is  
35 determined. In determining the annual standard deduction

1 factor, the department shall use the annual percent change,  
2 but not less than zero percent, in the implicit price deflator  
3 for the gross national product computed for the second quarter  
4 of the calendar year by the bureau of economic analysis of the  
5 United States department of commerce and shall add the total  
6 percent change to one hundred percent. The annual standard  
7 deduction factor and the cumulative standard deduction factor  
8 shall each be expressed as a percentage rounded to the nearest  
9 one-tenth of one percent. The annual standard deduction  
10 factor shall not be less than one hundred percent.

11 b. "Cumulative standard deduction factor" means the  
12 product of the annual standard deduction factor for the 1989  
13 calendar year and all annual standard deduction factors for  
14 subsequent calendar years as determined pursuant to this  
15 subsection. The cumulative standard deduction factor applies  
16 to all tax years beginning on or after January 1 of the  
17 calendar year for which the latest annual standard deduction  
18 factor has been determined.

19 c. The annual standard deduction factor for the 1989  
20 calendar year is one hundred percent.

21 d. Notwithstanding the computation of the annual standard  
22 deduction factor under paragraph "a", the annual standard  
23 deduction factor is one hundred percent for any calendar year  
24 beginning after December 31, 1990, in which the unobligated  
25 state general fund balance on June 30, as certified by the  
26 director of revenue and finance by October 10, is less than  
27 sixty million dollars.

28 Sec. 4. Section 422.5, Code 1989, is amended by adding the  
29 following new subsection:

30 NEW SUBSECTION. 10. In the case of income derived from  
31 the sale or exchange of livestock in excess of the number the  
32 taxpayer would sell if the taxpayer followed the taxpayer's  
33 usual business practices, a taxpayer may elect to spread the  
34 income equally over the four tax years following the tax year  
35 in which such sale or exchange occurs if the taxpayer

1 establishes that, under the taxpayer's usual business  
2 practices, the sale or exchange would not have occurred in the  
3 taxable year in which it occurred if it were not for drought  
4 conditions or other act of God. This subsection shall apply  
5 only to a taxpayer whose principal trade or business is  
6 farming, within the meaning of section 6420(c)(3), of the  
7 Internal Revenue Code.

8 Sec. 5. Section 422.9, subsection 6, unnumbered paragraph  
9 1, Code 1989, is amended by striking the unnumbered paragraph  
10 and inserting in lieu thereof the following:

11 The taxpayer may recompute the taxpayer's income tax  
12 liability for the tax year by subtracting from the taxpayer's  
13 taxable income, as computed without regard to this subsection,  
14 sixty percent of the net capital gain from the sale of the  
15 following:

16 a. Net capital gain from the sale of real property used in  
17 a business, in which the taxpayer materially participated, as  
18 defined in section 469(h) of the Internal Revenue Code, and  
19 which has been held for a minimum of ten years, or from the  
20 sale of a business in which the taxpayer was employed or in  
21 which the taxpayer materially participated, as defined in  
22 section 469(h) of the Internal Revenue Code, and which has  
23 been held for a minimum of ten years. The sale of a business  
24 means the sale of all or substantially all of the tangible  
25 personal property or services of the business.

26 b. Net capital gain from the sale of cattle or horses held  
27 by the taxpayer for breeding, draft, dairy, or sporting  
28 purposes for a period of twenty-four months or more from the  
29 date of acquisition; but only if the taxpayer received more  
30 than one-half of the taxpayer's gross income from farming or  
31 ranching operations in this state during the tax year.

32 c. Net capital gain from the sale of breeding livestock,  
33 other than cattle or horses, if the livestock is held by the  
34 taxpayer for a period of twelve months or more from the date  
35 of acquisition; but only if the taxpayer received more than

1 one-half of the taxpayer's gross income from farming or  
2 ranching operations in this state during the tax year.

3 d. The gain indicated in income for the tax year from the  
4 sale or exchange of livestock as described in section 422.5,  
5 subsection 10.

6 The net long-term capital gain of paragraphs "a", "b", "c",  
7 and "d" together shall not exceed seventeen thousand five  
8 hundred dollars for the tax year. Married taxpayers who elect  
9 separate filing on a combined return for state tax purposes  
10 are treated as one taxpayer and the amount of net capital gain  
11 to be used to determine the total amount to be subtracted by  
12 them shall not exceed seventeen thousand five hundred dollars  
13 in the aggregate. Married taxpayers who file jointly or  
14 separately on a combined return shall prorate the seventeen  
15 thousand five hundred dollar limitation between them based on  
16 the ratio of each spouse's net capital gain to the total net  
17 capital gain of both spouses. In the case of married  
18 taxpayers filing separate returns, the amount of net capital  
19 gain to be used to determine the amount to be subtracted by  
20 each spouse shall not exceed eight thousand seven hundred  
21 fifty dollars.

22 Sec. 6. Section 422.9, subsection 6, unnumbered paragraph  
23 4, Code 1989, is amended to read as follows:

24 For the tax year the total amount of refund claims that  
25 shall be paid shall not exceed eight million dollars. If the  
26 total amount of the claims for refund does exceed that amount,  
27 each claim for refund shall be paid on a pro rata basis so  
28 that the total amount paid for the tax year does not exceed  
29 eight million dollars. In the case where refund claims are  
30 not paid in full, the amount of the refund to which the  
31 taxpayer is entitled under this subsection is the pro rata  
32 amount that was paid and the taxpayer is not entitled to a  
33 refund for the unpaid portion and is not entitled to carry  
34 that amount forward or backward to another tax year.

35 Taxpayers shall not use refunds as estimated payments for the

1 succeeding tax year. Taxpayers whose tax years begin on  
2 January 1 must file their refund claims by October 31, 1986,  
3 to be eligible for refunds. Taxpayers whose tax years begin  
4 on a date in 1987 other than January 1 must file their refund  
5 claims by the end of the sixth month following the end of  
6 their tax years. The department shall determine on February  
7 17, 1989, if the total amount of claims for refund exceeds  
8 eight million dollars for the tax year. Notwithstanding any  
9 other provision, interest shall not be due on any refund  
10 claims that are paid by February 28, 1989. If the claim is  
11 not payable on February 28, 1989, because the taxpayer is a  
12 fiscal year filer, then the amount of the claim allowed shall  
13 be in the same ratio as refund claims available on February 17  
14 1989. These claims shall be funded by moneys appropriated for  
15 payment of refunds of individual income tax. The deadline for  
16 filing a claim for a refund for calendar year taxpayers whose  
17 tax years begin on January 1 is October 31 following the  
18 calendar year. The department shall determine on February 1  
19 following the October 31 deadline, if the total amount of  
20 claims for refund exceeds eight million dollars for the tax  
21 year. Notwithstanding any other provision, interest shall not  
22 be due on any refund claims that are paid by February 28  
23 following the October 31 deadline. Taxpayers whose tax years  
24 begin on a date other than January 1 must file their refund  
25 claims by the end of the sixth month following the end of  
26 their tax years. If the claim is not payable on February 28  
27 following the October 31 deadline of calendar year taxpayers,  
28 because the taxpayer is a fiscal year filer, then the amount  
29 of the claim allowed shall be the same ratio as refund claims  
30 available February 1 following the October 31 deadline. These  
31 claims shall be funded by moneys appropriated for payment of  
32 refunds of individual income tax.

33 Sec. 7. NEW SECTION. 422.12B EARNED INCOME TAX CREDIT.

34 1. The taxes imposed under this division, less credits  
35 allowed under sections 422.10 through 422.12, shall be reduced

1 by an earned income credit equal to ten percent of the federal  
2 earned income credit received by the taxpayer under section  
3 32(b) of the Internal Revenue Code. Any credit in excess of  
4 the tax liability is nonrefundable.

5 2. Married taxpayers electing to file separate returns or  
6 filing separately on a combined return may avail themselves of  
7 the earned income credit by allocating the earned income  
8 credit to each spouse in the proportion that each spouse's  
9 respective earned income bears to the total combined earned  
10 income. Taxpayers affected by the allocation provisions of  
11 section 422.8 shall be permitted a deduction for the credit  
12 only in the amount fairly and equitably allocable to Iowa  
13 under rules prescribed by the director.

14 Sec. 8. Section 422.21, Code 1989, is amended by adding  
15 the following new unnumbered paragraph:

16 NEW UNNUMBERED PARAGRAPH. The director shall determine for  
17 the 1990 and each subsequent calendar year the annual and  
18 cumulative standard deduction factors for each calendar year  
19 to be applied to tax years beginning on or after January 1 of  
20 that calendar year. The director shall compute the new  
21 standard deduction dollar amounts as specified in section  
22 422.9, subsection 1, by the latest cumulative standard  
23 deduction factor and round off the result to the nearest ten  
24 dollars. The annual and cumulative standard deduction factors  
25 determined by the director are not rules as defined in section  
26 17A.2, subsection 7.

27 Sec. 9. Section 1 of this Act takes effect January 1,  
28 1991, for tax years beginning on or after that date.

29 Sec. 10. Sections 2 and 3 of this Act take effect January  
30 1, 1990, for tax years beginning on or after that date.

31 Sec. 11. Sections 4, 5, 6, and 7 of this Act apply  
32 retroactively to January 1, 1989, for tax years beginning on  
33 or after that date.

34  
35

## SENATE FILE 537

H-4387

1 Amend amendment, H-4349, to Senate File 537, as  
2 amended, passed, and reprinted by the Senate, as  
3 follows:

4 1. Page 1, by inserting before line 44, the  
5 following:

6 "e. Net capital gain from the sale of stock or  
7 securities as defined in section 1083(f) of the  
8 Internal Revenue Code."

9 2. Page 1, line 45, by striking the words "and  
10 "d" and inserting the following: "'d", and "e".

BY METCALF OF Polk

H-4387 FILED MAY 2, 1989

lost 5-3-89 (p. 239A)

## SENATE FILE 537

H-4359

1 Amend amendment, H-4349, to Senate File 537, as  
2 amended, passed, and reprinted by the Senate, as  
3 follows:

4 1. By striking page 1, line 5, through page 2,  
5 line 25, and inserting the following:

6 ""Section 1. Section 422.5, subsection 1,  
7 paragraph k, unnumbered paragraph 2, Code 1989, is  
8 amended to read as follows:

9 The state alternative minimum taxable income of a  
10 taxpayer is equal to the taxpayer's state taxable  
11 income, as computed with the deductions in section  
12 422.9, ~~except for the net capital gain deduction~~, with  
13 the following adjustments:

14 Sec. 2. Section 422.9, subsection 6, Code 1989, is  
15 amended by striking the subsection.

16 Sec. 3. Section 422.21, unnumbered paragraph 6,  
17 Code 1989, is amended by striking the unnumbered  
18 paragraph."

19 2. Page 2, line 30, by striking the word "giving"  
20 and inserting the following: "eliminating the".

21 3. Page 2, line 31, by striking the words  
22 "treatment to limited amounts of capital gain,".

By CONNOLLY of Dubuque  
DODERER of Johnson

H-4359 FILED MAY 2, 1989

Lost 5-3-89 (p.2392)

## SENATE FILE 537

H-4368

1 Amend the amendment, H-4349, to Senate File 537, as  
2 amended, passed, and reprinted by the Senate, as  
3 follows:

4 1. Page 1, line 18, by striking the word "ten"  
5 and inserting the following: "five".

6 2. Page 1, line 23, by striking the word "ten"  
7 and inserting the following: "five".

By STROMER of Hancock

H-4368 FILED MAY 2, 1989

Withdrawn 5-3-89 (p.2391)

SENATE FILE 537

H-4349

1 Amend Senate File 537, as amended, passed, and  
2 reprinted by the Senate, as follows:

3 1. By striking everything after the enacting  
4 clause and inserting the following:

5 "Section 1. Section 422.9, subsection 6,  
6 unnumbered paragraph 1, Code 1989, is amended by  
7 striking the paragraph and inserting in lieu thereof  
8 the following:

9 The taxpayer may recompute the taxpayer's income  
10 tax liability for the tax year by subtracting from the  
11 taxpayer's taxable income, as computed without regard  
12 to this subsection, sixty percent of the net capital  
13 gain from the sale of the following:

14 a. Net capital gain from the sale of real property  
15 used in a business, in which the taxpayer materially  
16 participated for ten years, as defined in section  
17 469(h) of the Internal Revenue Code, and which has  
18 been held for a minimum of ten years, or from the sale  
19 of a business, as defined in section 422.42, in which  
20 the taxpayer was employed or in which the taxpayer  
21 materially participated for ten years, as defined in  
22 section 469(h) of the Internal Revenue Code, and which  
23 has been held for a minimum of ten years. The sale of  
24 a business means the sale of all or substantially all  
25 of the tangible personal property or service of the  
26 business.

27 b. Net capital gain from the sale of cattle or  
28 horses held by the taxpayer for breeding, draft,  
29 dairy, or sporting purposes for a period of twenty-  
30 four months or more from the date of acquisition; but  
31 only if the taxpayer received more than one-half of  
32 the taxpayer's gross income from farming or ranching  
33 operations during the tax year.

34 c. Net capital gain from the sale of breeding  
35 livestock, other than cattle or horses, if the  
36 livestock is held by the taxpayer for a period of  
37 twelve months or more from the date of acquisition;  
38 but only if the taxpayer received more than one-half  
39 of the taxpayer's gross income from farming or  
40 ranching operations during the tax year.

41 d. Net capital gain from the sale of timber as  
42 defined in section 631(a) of the Internal Revenue  
43 Code.

44 The net capital gain of paragraphs "a", "b", "c",  
45 and "d" together shall not exceed seventeen thousand  
46 five hundred dollars for the tax year. Married  
47 taxpayers who elect separate filing on a combined  
48 return for state tax purposes are treated as one  
49 taxpayer and the amount of net capital gain to be used  
50 to determine the total amount to be subtracted by them

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1 shall not exceed seventeen thousand five hundred  
2 dollars in the aggregate. Married taxpayers who file  
3 jointly or separately on a combined return shall  
4 prorate the seventeen thousand five hundred dollar  
5 limitation between them based on the ratio of each  
6 spouse's net capital gain to the total net capital  
7 gain of both spouses. In the case of married  
8 taxpayers filing separate returns, the amount of net  
9 capital gain to be used to determine the amount to be  
10 subtracted by each spouse shall not exceed eight  
11 thousand seven hundred fifty dollars.

4404 12 Sec. 2. Section 422.21, unnumbered paragraph 6,  
13 Code 1989, is amended to read as follows:

14 The department shall prepare and make available a  
15 special return for filing a tax refund claim resulting  
16 from the net capital gain deduction authorized in  
17 section 422.9, subsection 6. ~~The special returns  
18 shall be designed so that the department will be able  
19 to compile data that identifies the source and type of  
20 the capital gains and losses and the geographical  
21 location of the transactions involving the capital  
22 gains and losses. By January 15, 1989, the department  
23 shall make available to the general assembly the data  
24 compiled from the special returns filed during the  
25 previous calendar year.~~

4403 26 Sec. 3. This Act is retroactively applicable for  
27 tax years beginning on or after January 1, 1989."

28 2. Title page, by striking lines 1 through 5 and  
29 inserting the following: "An Act relating to state  
30 individual income tax by giving capital gain deduction  
31 treatment to limited amounts of capital gain, and  
4404 32 providing a retroactive applicability date."

By COMMITTEE ON WAYS AND MEANS  
TABOR of Jackson, Chairperson

H-4349 FILED MAY 1, 1989

SENATE FILE 537

H-4349

1 Amend Senate File 537, as amended, passed, and  
2 reprinted by the Senate, as follows:

3 1. By striking everything after the enacting  
4 clause and inserting the following:

4357 5 "Section 1. Section 422.9, subsection 6,  
6 unnumbered paragraph 1, Code 1989, is amended by  
7 striking the paragraph and inserting in lieu thereof  
8 the following:

9 The taxpayer may recompute the taxpayer's income  
10 tax liability for the tax year by subtracting from the  
11 taxpayer's taxable income, as computed without regard  
12 to this subsection, sixty percent of the net capital  
13 gain from the sale of the following:

4368 14 a. Net capital gain from the sale of real property  
15 used in a business, in which the taxpayer materially  
16 participated for ten years, as defined in section  
17 469(h) of the Internal Revenue Code, and which has  
18 been held for a minimum of ten years, or from the sale  
19 of a business, as defined in section 422.42, in which  
20 the taxpayer was employed or in which the taxpayer  
21 materially participated for ten years, as defined in  
22 section 469(h) of the Internal Revenue Code, and which  
23 has been held for a minimum of ten years. The sale of  
24 a business means the sale of all or substantially all  
25 of the tangible personal property or service of the  
26 business.

27 b. Net capital gain from the sale of cattle or  
28 horses held by the taxpayer for breeding, draft,  
29 dairy, or sporting purposes for a period of twenty-  
30 four months or more from the date of acquisition; but  
31 only if the taxpayer received more than one-half of  
32 the taxpayer's gross income from farming or ranching  
33 operations during the tax year.

34 c. Net capital gain from the sale of breeding  
35 livestock, other than cattle or horses, if the  
36 livestock is held by the taxpayer for a period of  
37 twelve months or more from the date of acquisition;  
38 but only if the taxpayer received more than one-half  
39 of the taxpayer's gross income from farming or  
40 ranching operations during the tax year.

41 d. Net capital gain from the sale of timber as  
42 defined in section 631(a) of the Internal Revenue  
43 Code.

43, 47 44 The net capital gain of paragraphs "a", "b", "c",  
45 and "d" together shall not exceed seventeen thousand  
46 five hundred dollars for the tax year. Married  
47 taxpayers who elect separate filing on a combined  
48 return for state tax purposes are treated as one  
49 taxpayer and the amount of net capital gain to be used  
50 to determine the total amount to be subtracted by them

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1 shall not exceed seventeen thousand five hundred  
 2 dollars in the aggregate. Married taxpayers who file  
 3 jointly or separately on a combined return shall  
 4 prorate the seventeen thousand five hundred dollar  
 5 limitation between them based on the ratio of each  
 6 spouse's net capital gain to the total net capital  
 7 gain of both spouses. In the case of married  
 8 taxpayers filing separate returns, the amount of net  
 9 capital gain to be used to determine the amount to be  
 10 subtracted by each spouse shall not exceed eight  
 11 thousand seven hundred fifty dollars.

4357 12 Sec. 2. Section 422.21, unnumbered paragraph 6,  
 13 Code 1989, is amended to read as follows:

14 The department shall prepare and make available a  
 15 special return for filing a tax refund claim resulting  
 16 from the net capital gain deduction authorized in  
 17 section 422.9, subsection 6. ~~The special returns~~  
 18 ~~shall be designed so that the department will be able~~  
 19 ~~to compile data that identifies the source and type of~~  
 20 ~~the capital gains and losses and the geographical~~  
 21 ~~location of the transactions involving the capital~~  
 22 ~~gains and losses. -- By January 15, 1989, the department~~  
 23 ~~shall make available to the general assembly the data~~  
 24 ~~compiled from the special returns filed during the~~  
 25 ~~previous calendar year.~~

26 Sec. 3. This Act is retroactively applicable for  
 27 tax years beginning on or after January 1, 1989."

4359 28 2. Title page, by striking lines 1 through 5 and  
 29 inserting the following: "An Act relating to state  
 30 individual income tax by giving capital gain deduction  
 31 treatment to limited amounts of capital gain, and  
 32 providing a retroactive applicability date."

By COMMITTEE ON WAYS AND MEANS  
 TABOR of Jackson, Chairperson

H-4349 FILED MAY 1, 1989

Adopted 5-3-89 (p. 2392)

SENATE FILE 537

H-4404

1 Amend amendment, H-4349, to Senate file 537, as  
2 amended, passed, and reprinted by the Senate, as  
3 follows:

4 1. Page 1, by inserting before line 5, the  
5 following:

6 "Sec. 100. Section 422.4, subsection 17, paragraph  
7 c, Code 1989, is amended to read as follows:

8 c. The annual inflation factor for the 1988  
9 calendar year is one hundred percent. The annual  
10 inflation factor for the 1990 calendar year is one  
11 hundred percent, notwithstanding the computation under  
12 paragraph "a".

13 Sec. 101. Section 422.4, subsection 17, Code 1989,  
14 is amended by adding the following new paragraph:

15 NEW PARAGRAPH. e. If for a calendar year,  
16 paragraph "d" does not require the annual inflation  
17 factor to be equal to one hundred percent then the  
18 annual inflation factor is as computed under paragraph  
19 "a" unless the most recent increase in adjustment for  
20 inflation was to the tax brackets rather than the  
21 standard deduction in which case the annual inflation  
22 factor is one hundred percent. For purposes of this  
23 paragraph, the increase in the standard deduction  
24 amounts for tax years beginning in the 1990 calendar  
25 year is deemed to be an increase in adjustment for  
26 inflation.

27 Sec. 102. Section 422.5, subsection 7, Code 1989,  
28 is amended to read as follows:

29 7. a. Upon determination of the latest cumulative  
30 inflation factor, the director shall multiply each  
31 dollar amount of the tax brackets set forth in  
32 subsection 1, paragraphs "a" and through "i" of this  
33 section, and each dollar amount specified in this  
34 section as the maximum amount of annuities received  
35 which may be excluded in determining final taxable  
36 income, by this cumulative inflation factor, shall  
37 round off the resulting product to the nearest one  
38 dollar, and shall incorporate the result into the  
39 income tax forms and instructions for each tax year.

40 b. If the tax brackets for a tax year would have  
41 been adjusted except for the operation of section  
42 422.4, subsection 17, paragraph "e", the director  
43 shall adjust for inflation the standard deduction  
44 amounts specified in section 422.9, subsection 1, as  
45 may have been previously adjusted under this  
46 paragraph. In determining the amount of adjustment in  
47 each dollar amount of the standard deductions, the  
48 director shall estimate by October 15 the fiscal  
49 impact on state revenues if the tax brackets would  
50 have been adjusted, except for the operation of

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1 section 422.4, subsection 17, paragraph "e". The  
2 director shall then determine the amount of adjustment  
3 in each dollar amount of the standard deductions which  
4 will result in the same fiscal impact on state  
5 revenues for the tax year as if the tax brackets had  
6 been adjusted. The same percentage amount of  
7 adjustment shall be made in each dollar amount of the  
8 standard deductions. Any adjustment in the standard  
9 deductions as a result of this paragraph shall  
10 continue for subsequent tax years until otherwise  
11 adjusted as provided in this paragraph or other  
12 provision of law.

13 Sec. 103. Section 422.9, subsection 1, Code 1989,  
14 is amended to read as follows:

15 1. An optional standard deduction, after deduction  
16 of federal income tax, equal to one thousand ~~two~~ four  
17 hundred ~~thirty~~ dollars for a married person who files  
18 separately or a single person or equal to three  
19 thousand ~~thirty~~ four hundred fifty dollars for a  
20 husband and wife who file a joint return, a surviving  
21 spouse, or an unmarried head of household. The  
22 optional standard deduction shall not exceed the  
23 amount remaining after deduction of the federal income  
24 tax."

25 2. Page 2, by inserting before line 12 the  
26 following:

27 "Sec. 104. Section 422.21, unnumbered paragraph 4,  
28 Code 1989, is amended to read as follows:

29 The director shall determine for the 1989 and each  
30 subsequent calendar year the annual and cumulative  
31 inflation factors for each calendar year to be applied  
32 to tax years beginning on or after January 1 of that  
33 calendar year. The director shall compute the new  
34 dollar amounts as specified to be adjusted in section  
35 422.5 by the latest cumulative inflation factor and  
36 round off the result to the nearest one dollar. The  
37 annual and cumulative inflation factors determined by  
38 the director are not rules as defined in section  
39 17A.2, subsection 7. The director shall determine for  
40 the 1992 and each subsequent calendar year if an  
41 adjustment in the standard deductions, as provided in  
42 section 422.5, subsection 7, paragraph "b", are  
43 required for tax years beginning in that calendar  
44 year. The amount of any adjustment in the standard  
45 deductions determined by the director are not rules as  
46 defined in section 17A.2, subsection 7."

47 3. Page 2, by striking lines 26 and 27 and in-  
48 serting the following:

49 "Sec. \_\_\_\_ . Sections 1 and 2 of this Act retro-  
50 actively apply to tax years beginning on or after

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1 January 1, 1989.

2 Sec. \_\_\_\_ . Sections 100 and 103 of this Act apply  
3 to tax years beginning on or after January 1, 1990.4 Sec. \_\_\_\_ . Sections 101 and 102 of this Act apply  
5 to tax years beginning on or after January 1, 1991."6 4. Page 2, line 29, by inserting after the word  
7 "Act" the following: "relating to the indexing of tax  
8 brackets and the standard deduction for income tax  
9 purposes, increasing the amount of the standard  
10 deduction,".11 5. Page 2, by striking line 32 and inserting the  
12 following: "providing certain applicability dates."

13 6. Renumber as necessary.

By TABOR of Jackson

H-4404 FILED MAY 3, 1989

ADOPTED

5.389 (P. 2391)

SENATE FILE 537  
H-4404 TO H-4369 TO SENATE FILE 537  
FISCAL NOTE

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A fiscal note for H-4404 TO H-4349 TO SENATE FILE 537 is hereby submitted pursuant to Joint Rule 17. Data used in developing this available from the Legislative Fiscal Bureau to members of the Legislature upon request.

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H-4404 to H-4349 to Senate File 537 does the following: (a) increases current standard deduction amounts by 14%, \$1,230 is raised to \$1,400 and \$3,030 is raised to \$3,450 effective for tax years 1990 and beyond; (b) except for tax year 1990, retains the trigger for indexation based on the size of the General Fund ending balance; (c) for subsequent tax years, if indexation is triggered, brackets will be indexed as they are currently indexed, unless brackets were indexed previously, in which case the department is to determine the fiscal effect of indexing brackets and then instead standard deduction amounts will be increased by sufficient amounts to reduce taxpayer liability by the same amount that would have occurred under bracket indexation.

Fiscal Effect

The effect of increasing the standard deduction amounts for tax year 1990, is estimated to be a \$9.7 million reduction in taxpayer liability. Under current law, if indexation of brackets were triggered for tax year 1990, the reduction in taxpayer liability is estimated to be \$9.9 million.

For subsequent years, when indexation is triggered, this amendment will not have a different effect on the General Fund in terms of the total amount of reduction to the General Fund, since further standard deduction increases would be designed to have the same fiscal impact of bracket indexation.

Source: Legislative Tax Model

(LSB 2721sv.2, PDD)

FILED MAY 3, 1989

BY DENNIS PROUTY, FISCAL DIRECTOR

HOUSE AMENDMENT TO  
SENATE FILE 537

S-4106

1 Amend Senate File 537, as amended, passed, and  
2 reprinted by the Senate, as follows:

3 1. By striking everything after the enacting  
4 clause and inserting the following:

5 Section 100. Section 422.4, subsection 17,  
6 paragraph c, Code 1989, is amended to read as follows:

7 c. The annual inflation factor for the 1988  
8 calendar year is one hundred percent. The annual  
9 inflation factor for the 1990 calendar year is one  
10 hundred percent, notwithstanding the computation under  
11 paragraph "a".

12 Sec. 101. Section 422.4, subsection 17, Code 1989,  
13 is amended by adding the following new paragraph:

14 NEW PARAGRAPH. d. If for a calendar year,  
15 paragraph "d" does not require the annual inflation  
16 factor to be equal to one hundred percent then the  
17 annual inflation factor is as computed under paragraph  
18 "a" unless the most recent increase in adjustment for  
19 inflation was to the tax brackets rather than the  
20 standard deduction in which case the annual inflation  
21 factor is one hundred percent. For purposes of this  
22 paragraph, the increase in the standard deduction  
23 amounts for tax years beginning in the 1990 calendar  
24 year is deemed to be an increase in adjustment for  
25 inflation.

26 Sec. 102. Section 422.5, subsection 7, Code 1989,  
27 is amended to read as follows:

28 7. a. Upon determination of the latest cumulative  
29 inflation factor, the director shall multiply each  
30 dollar amount of the tax brackets set forth in  
31 subsection 1, paragraphs "a" and through "i" of this  
32 section, and each dollar amount specified in this  
33 section as the maximum amount of annuities received  
34 which may be excluded in determining final taxable  
35 income, by this cumulative inflation factor, shall  
36 round off the resulting product to the nearest one  
37 dollar, and shall incorporate the results into the  
38 income tax forms and instructions for each tax year.

39 b. If the tax brackets for a tax year would have  
40 been adjusted except for the operation of section  
41 422.4, subsection 17, paragraph "e", the director  
42 shall adjust for inflation the standard deduction  
43 amounts specified in section 422.9, subsection 1, as  
44 may have been previously adjusted under this  
45 paragraph. In determining the amount of adjustment to  
46 each dollar amount of the standard deductions, the  
47 director shall estimate by October 15 the fiscal  
48 impact on state revenues if the tax brackets would  
49 have been adjusted, except for the operation of  
50 section 422.4, subsection 17, paragraph "a". The

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1 director shall then determine the amount of adjustment  
 2 in each dollar amount of the standard deductions which  
 3 will result in the same fiscal impact on state  
 4 revenues for the tax year as if the tax brackets had  
 5 been adjusted. The same percentage amount of  
 6 adjustment shall be made in each dollar amount of the  
 7 standard deductions. Any adjustment in the standard  
 8 deductions as a result of this paragraph shall  
 9 continue for subsequent tax years until otherwise  
 10 adjusted as provided in this paragraph or other  
 11 provision of law.

4109 12 Sec. 103. Section 422.9, subsection 1, Code 1989,  
 13 is amended to read as follows:

14 1. An optional standard deduction, after deduction  
 15 of federal income tax, equal to one thousand two hundred  
 16 hundred thirty dollars for a married person who files  
 17 separately or a single person or equal to three  
 18 thousand three hundred forty five dollars for a  
 19 husband and wife who file a joint return, a surviving  
 20 spouse, or an unmarried head of household. The  
 21 optional standard deduction shall not exceed the  
 22 amount remaining after deduction of the federal income  
 23 tax.

24 Sec. 2. Section 422.9, subsection 6, unnumbered  
 25 paragraph 1, Code 1989, is amended by striking the  
 26 paragraph and inserting in lieu thereof the following:

27 The taxpayer may recompute the taxpayer's income  
 28 tax liability for the tax year by subtracting from the  
 29 taxpayer's taxable income, as computed without regard  
 30 to this subsection, sixty percent of the net capital  
 31 gain from the sale of the following:

32 a. Net capital gain from the sale of real property  
 33 used in a business, in which the taxpayer materially  
 34 participated for ten years, as defined in section  
 35 469(c) of the Internal Revenue Code, and which has  
 36 been held for a minimum of ten years, or from the sale  
 37 of a business, as defined in section 422.42, in which  
 38 the taxpayer was employed or in which the taxpayer  
 39 materially participated for ten years, as defined in  
 40 section 469(h) of the Internal Revenue Code, and which  
 41 has been held for a minimum of ten years. The sale of  
 42 a business means the sale of all or substantially all  
 43 of the tangible personal property or service of the  
 44 business.

45 b. Net capital gain from the sale of cattle or  
 46 horses held by the taxpayer for breeding, show,  
 47 dairy, or sporting purposes for a period of twenty  
 48 four months or more from the date of acquisition and  
 49 only if the taxpayer received more than one-half of  
 50 the taxpayer's gross income from farming or ranching

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1 operations during the tax year.

2 c. Net capital gain from the sale of breeding  
3 livestock, other than cattle or horses, if the  
4 livestock is held by the taxpayer for a period of  
5 twelve months or more from the date of acquisition;  
6 but only if the taxpayer received more than one-half  
7 of the taxpayer's gross income from farming or  
8 ranching operations during the tax year.

9 d. Net capital gain from the sale of timber as  
10 defined in section 631(a) of the Internal Revenue  
11 Code.

12 The net capital gain of paragraphs "a", "b", "c",  
13 and "d" together shall not exceed seventeen thousand  
14 five hundred dollars for the tax year. Married  
15 taxpayers who elect separate filing on a combined  
16 return for state tax purposes are treated as one  
17 taxpayer and the amount of net capital gain to be used  
18 to determine the total amount to be subtracted by them  
19 shall not exceed seventeen thousand five hundred  
20 dollars in the aggregate. Married taxpayers who file  
21 jointly or separately on a combined return shall  
22 prorate the seventeen thousand five hundred dollar  
23 limitation between them based on the ratio of each  
24 spouse's net capital gain to the total net capital  
25 gain of both spouses. In the case of married  
26 taxpayers filing separate returns, the amount of net  
27 capital gain to be used to determine the amount to be  
28 subtracted by each spouse shall not exceed eight  
29 thousand seven hundred fifty dollars.

30 Sec. 104. Section 422.21, unnumbered paragraph 4,  
31 Code 1989, is amended to read as follows:

32 The director shall determine for the 1989 and each  
33 subsequent calendar year the annual and cumulative  
34 inflation factors for each calendar year to be applied  
35 to tax years beginning on or after January 1 of each  
36 calendar year. The director shall compute the new  
37 dollar amounts as specified to be adjusted in section  
38 422.5 by the latest cumulative inflation factor and  
39 round off the result to the nearest one dollar. The  
40 annual and cumulative inflation factors determined by  
41 the director are not rules as defined in section  
42 17A.2, subsection 7. The director shall determine for  
43 the 1992 and each subsequent calendar year if an  
44 adjustment in the standard deductions, as provided in  
45 section 422.5, subsection 7, paragraph "b", are  
46 required for tax years beginning in that calendar  
47 year. The amount of any adjustment in the standard  
48 deductions determined by the director are not rules as  
49 defined in section 17A.2, subsection 7.

50 Sec. 3. Section 422.21, unnumbered paragraph 5,

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1 Code 1989, is amended to read as follows:

2 The department shall prepare and make available a  
 3 special return for filing a tax refund claim resulting  
 4 from the net capital gain deduction authorized in  
 5 section 422.9, subsection 6. ~~The special returns  
 6 shall be designed so that the department will be able  
 7 to compile data that identifies the source and type of  
 8 the capital gains and losses and the geographical  
 9 location of the transactions involving the capital  
 10 gains and losses. By January 15, 1989, the department  
 11 shall make available to the general assembly the data  
 12 compiled from the special returns filed during the  
 13 previous calendar year.~~

4109 14 Sec. \_\_\_\_ . Sections 1 and 2 of this Act retro-  
 15 actively apply to tax years beginning on or after  
 16 January 1, 1989.

17 Sec. \_\_\_\_ . Sections 100 and 103 of this Act apply  
 18 to tax years beginning on or after January 1, 1990.

19 Sec. \_\_\_\_ . Sections 101 and 102 of this Act apply  
 20 to tax years beginning on or after January 1, 1991.

21 2. Title page, by striking lines 1 through 5 and  
 22 inserting the following: "An Act relating to the  
 4158 23 indexing of tax brackets and the standard deduction  
 4109 24 for income tax purposes, increasing the amount of the  
 25 standard deduction, relating to state individual  
 26 income tax by giving capital gain deduction treatment  
 27 to limited amounts of capital gain, and providing  
 28 certain applicability dates.

RECEIVED FROM THE HOUSE

S-4106 FILED MAY 4, 1989

*Adopted as amended 5/6 (p. 2083)*

## SENATE FILE 537

S-4109

1 Amend the amendment, S-4106, to Senate File 537, as  
2 amended, passed, and reprinted by the Senate, as  
3 follows:

4 1. Page 1, by inserting before line 26, the  
5 following:

6 "Section 210. Section 422.5, subsection 1, Code  
7 1989, is amended by adding the following new  
8 paragraph:

9 NEW PARAGRAPH. 1. The tax imposed upon the  
10 taxable income of a resident shareholder in a  
11 corporation which has in effect for the tax year an  
12 election under subchapter S of the Internal Revenue  
13 Code and carries on business within and without the  
14 state shall be computed by reducing the amount  
15 determined pursuant to paragraphs "a" through "i" by  
16 the amounts of nonrefundable credits under this  
17 division and multiplying this resulting amount by a  
18 fraction of which the resident's net income allocated  
19 to Iowa, as determined in section 422.8, subsection 5,  
20 is the numerator and the resident's total net income  
21 computed under section 422.7 is the denominator. This  
22 provision also applies to individuals who are  
23 residents of Iowa for less than the entire tax year.

24 Sec. 211. Section 422.5, subsection 1, paragraph  
25 k, subparagraph (3), unnumbered paragraph 3, Code  
26 1989, is amended to read as follows:

27 In the case of a resident, including a resident  
28 estate or trust, the state's apportioned share of the  
29 state alternative minimum tax is one hundred percent  
30 of the state alternative minimum tax computed in this  
31 subsection. In the case of a resident or part-year  
32 resident shareholder in a corporation which has in  
33 effect for the tax year an election under subchapter S  
34 of the Internal Revenue Code and carries on business  
35 within and without the state, a nonresident, including  
36 a nonresident estate or trust, or an individual,  
37 estate, or trust that is domiciled in the state for  
38 less than the entire tax year, the state's apportioned  
39 share of the state alternative minimum tax is the  
40 amount of tax computed under this subsection, reduced  
41 by the applicable credits in sections 422.10, 422.11,  
42 422.11A, and 422.12 and this result multiplied by a  
43 fraction with a numerator of the sum of state net  
44 income allocated to Iowa as determined in section  
45 422.8, subsection 2 or subsection 5, whichever is  
46 applicable, plus tax preference items, adjustments,  
47 and losses under subparagraph (1) attributable to Iowa  
48 and with a denominator of the sum of total net income  
49 computed under section 422.7 plus all tax preference  
50 items, adjustments, and losses under subparagraph (1).

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1 In computing this fraction, those items excludable  
2 under subparagraph (1) shall not be used in computing  
3 the tax preference items. Married taxpayers electing  
4 to file separate returns or separately on a combined  
5 return must allocate the minimum tax computed in this  
6 subsection in the proportion that each spouse's  
7 respective preference items, adjustments, and losses  
8 under subparagraph (1) bear to the combined preference  
9 items, adjustments, and losses under subparagraph (1)  
10 of both spouses."

11 2. Page 2, by inserting before line 12, the  
12 following:

13 "Sec. 212. Section 422.7, Code 1989, is amended by  
14 adding the following new subsection:

15 NEW SUBSECTION. 19. Resident shareholders of a  
16 corporation which has an election in effect under  
17 subchapter S of the Internal Revenue Code shall add  
18 their proportionate share of a deemed distribution of  
19 current year income to the extent that the salaries,  
20 wages, or other compensation for services performed of  
21 all shareholders does not equal ten percent of net  
22 income of the corporation computed in accordance with  
23 section 422.35 and considering items of income and  
24 expense which pass directly to the shareholders under  
25 provisions of the Internal Revenue Code before  
26 deduction of shareholders' salaries, wages, or other  
27 compensation for services performed. In addition  
28 there shall be added any cash or the value of any  
29 property distributions made to the extent they are  
30 made from income upon which Iowa income tax has not  
31 been paid as determined under rules of the director.

32 Sec. 213. Section 422.8, Code 1989, is amended by  
33 adding the following new subsection:

34 NEW SUBSECTION. 5. A resident's income allocable  
35 to Iowa is the income determined under section 422.7  
36 reduced by the net income of a corporation which is  
37 fairly and equitably attributable without the state  
38 under section 422.33. For the purposes of this  
39 subsection, "corporation" means a corporation which  
40 has in effect for the tax year an election under  
41 subchapter S of the Internal Revenue Code and carries  
42 on business partly within and partly without the  
43 state. This provision also applies to individuals who  
44 are residents of Iowa for less than the entire tax  
45 year."

46 3. Page 4, line 14, by striking the words "and 2"  
47 and inserting the following: ", 2, 210, 211, 212, and  
48 213".

49 4. Page 4, line 24, by inserting after the word  
50 "purposes," the following: "providing for income

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1 taxation for certain shareholders of subchapter S  
2 corporations,".

3 5. By renumbering as necessary.

By CALVIN O. HULTMAN

## SENATE FILE 537

S-4188

1 Amend the House amendment, S-4106 to Senate File  
2 537, as amended, passed, and reprinted by the Senate,  
3 as follows:  
4 1. By striking page 1, line 5, through page 2,  
5 line 31, and inserting the following:  
6 "Sec. 300. Section 422.4, Code 1989, is amended by  
7 adding the following new subsection:  
8 NEW SUBSECTION. 18. a. "Annual standard  
9 deduction factor" means an index, expressed as a  
10 percentage, determined by the department by October 15  
11 of the calendar year preceding the calendar year for  
12 which the factor is determined, which reflects the  
13 purchasing power of the dollar as a result of  
14 inflation during the fiscal year ending in the  
15 calendar year preceding the calendar year for which  
16 the factor is determined. In determining the annual  
17 standard deduction factor, the department shall use  
18 the annual percent change, but not less than zero  
19 percent, in the implicit price deflator for the gross  
20 national product computed for the second quarter of  
21 the calendar year by the bureau of economic analysis  
22 of the United States department of commerce and shall  
23 add one-half of that percent change to one hundred  
24 percent. The annual standard deduction factor and the  
25 cumulative standard deduction factor shall each be  
26 expressed as a percentage rounded to the nearest one-  
27 tenth of one percent. The annual standard deduction  
28 factor shall not be less than one hundred percent.  
29 b. "Cumulative standard deduction factor" means  
30 the product of the annual standard deduction factor  
31 for the 1989 calendar year and all annual standard  
32 deduction factors for subsequent calendar years as  
33 determined pursuant to this subsection. The  
34 cumulative standard deduction factor applies to all  
35 tax years beginning on or after January 1 of the  
36 calendar year for which the latest annual standard  
37 deduction factor has been determined.  
38 c. The annual standard deduction factor for the  
39 1989 calendar year is one hundred percent.  
40 Sec. 400. Section 422.5, subsection 1, paragraph  
41 k, unnumbered paragraph 2, Code 1989, is amended to  
42 read as follows:  
43 The state alternative minimum taxable income of a  
44 taxpayer is equal to the taxpayer's state taxable  
45 income, as computed with the deductions in section  
46 422.9, ~~except for the net capital gain deduction,~~ with  
47 the following adjustments:  
48 Sec. 401. Section 422.5, Code 1989, is amended by  
49 adding the following new subsection:  
50 NEW SUBSECTION. 10. In the case of income derived

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1 from the sale or exchange of livestock which qualifies  
2 under section 451(e) of the Internal Revenue Code  
3 because of drought, the taxpayer may elect to include  
4 the income in the taxpayer's net income in the tax  
5 year following the year of the sale or exchange in  
6 accordance with rules prescribed by the director.

7 Sec. 402. Section 422.7, Code 1989, is amended by  
8 adding the following new subsection:

9 "NEW SUBSECTION. 19. Subtract forty-five percent  
10 of the net capital gain from the following:"

11 2. Page 3, by inserting before line 30 the  
12 following:

13 "Sec. 403. Section 422.9, subsection 6, Code 1989,  
14 is amended by striking the subsection.

15 Sec. 301. NEW SECTION. 422.12B EARNED INCOME TAX  
16 CREDIT.

17 1. The taxes imposed under this division, less  
18 credits allowed under sections 422.10 through 422.12,  
19 shall be reduced by an earned income credit equal to  
20 five percent of the federal earned income credit  
21 received by the taxpayer under section 32(b) of the  
22 Internal Revenue Code. Any credit in excess of the  
23 tax liability is nonrefundable.

24 2. Married taxpayers electing to file separate  
25 returns or filing separately on a combined return may  
26 avail themselves of the earned income credit by  
27 allocating the earned income credit to each spouse in  
28 the proportion that each spouse's respective earned  
29 income bears to the total combined earned income.  
30 Taxpayers affected by the allocation provisions of  
31 section 422.8 shall be permitted a deduction for the  
32 credit only in the amount fairly and equitably  
33 allocable to Iowa under rules prescribed by the  
34 director."

35 3. By striking page 3, line 43 through page 4,  
36 line 20, and inserting the following: "the 1990  
37 calendar year and each subsequent calendar year the  
38 annual and cumulative standard deduction factors to be  
39 applied to tax years beginning on or after January 1  
40 of that calendar year. The director shall compute the  
41 new dollar amounts of the standard deductions  
42 specified in section 422.9, subsection 1, by the  
43 latest cumulative standard deduction factor and round  
44 off the result to the nearest ten dollars. The annual  
45 and cumulative standard deduction factors determined  
46 by the director are not rules as defined in section  
47 17A.2, subsection 7.

48 Sec. 404. Section 422.21, unnumbered paragraph 6,  
49 Code 1989, is amended by striking the unnumbered  
50 paragraph.

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1 Sec. \_\_\_\_\_. Sections 300, 301, and 104 of this Act  
2 apply to tax years beginning on or after January 1,  
3 1990.

4 Sec. \_\_\_\_\_. Sections 400, 401, 402, 403, and 404 of  
5 this Act apply retroactively to January 1, 1989, for  
6 tax years beginning on or after that date."

7 4. Page 4, line 23, by striking the words "tax  
8 brackets and".

9 5. Page 4, lines 24 and 25, by striking the words  
10 ", increasing the amount of the standard deduction"  
11 and inserting the following: "providing an earned  
12 income tax credit".

By CHARLES BRUNER  
BILL HUTCHINS  
BILL DIELEMAN

S-4188 FILED MAY 6, 1989

LOST, RECONSIDERED & ADOPTED (p. 2083)  
(p. 2071)

SENATE FILE 537

S-4189

1 Amend amendment S-4188 to the House amendment, S-4106,  
2 to Senate File 537, as amended, passed, and reprinted by the  
3 Senate as follows:

4 1. Page 3, by striking lines 5 and 6 and inserting in  
5 lieu thereof the following: "this Act apply to tax years  
6 beginning on or after January 1, 1990."

By CHARLES BRUNER

S-4189 FILED MAY 6, 1989

ADOPTED (p. 2071)

SENATE FILE 537  
FISCAL NOTE

A fiscal note for S-4106 TO SENATE FILE 537 is hereby submitted pursuant to Joint Rule 17. Data used in developing this fiscal note is available from the Legislative Fiscal Bureau to members of the Legislature upon request.

S-4106 to Senate File 537 strikes everything after the enacting clause then adds provisions relating to the standard deduction amounts, indexation and the capital gains refund program.

Standard deduction increases: The amendment increases current standard deduction amounts by 14%; \$1,230 is raised to \$1,400 and \$3,030 is raised to \$3,450 effective for tax years 1990 and beyond.

Indexation: For tax year 1990, the trigger for indexation based on the size of the General Fund ending balance will not operate. For tax years 1991 and beyond the trigger mechanism will again be operational. If indexation is triggered for tax years 1991 and beyond, brackets will be indexed as they are currently indexed, unless brackets were indexed previously, in which case the department is to determine the fiscal effect of indexing brackets and then instead standard deduction amounts will be increased by sufficient amounts to reduce taxpayer liability by the same amount that would have occurred under bracket indexation.

Capital Gains Refund Program: Beginning tax year 1989, only certain types of assets would be eligible for the 60% capital gains deduction refund. Generally the eligible assets must be (a) real property used in a business, in which the taxpayer materially participated, or was employed, and which was held for a minimum of 10 years, or (b) from the sale of livestock by taxpayers deriving more than half of their income from farming or ranching, or (c) from the sale of timber meeting certain I.R.S. guidelines. The \$8.0 million cap on the total amount refunded would continue.

Fiscal Effect

The effect of increasing the standard deduction amounts for tax year 1990, is estimated to be a \$9.7 million reduction in taxpayer liability. Assuming the Department does not change withholding tables for tax year 1990, this effect would occur in FY 1991. Under current law, if indexation of brackets were triggered for tax year 1990, the reduction in taxpayer liability is estimated to be \$9.9 million.

For subsequent years, when indexation is triggered, this amendment will not have a different effect on the General Fund in terms of the total amount of reduction to the General Fund, since further standard deduction increases would be designed to have the same fiscal impact of bracket indexation.

Source: Legislative Tax Model

SENATE FILE 537  
FISCAL NOTE

REQ. BY SENATOR BRUNER

A fiscal note for S-4188 is hereby submitted pursuant to Joint Rule 17. Data used in developing this fiscal note is available from the Legislative Fiscal Bureau to members of the Legislature upon request.

S-4188 to Senate File 537 changes the capital gains refund program to an exemption targeted to specific types of gains, creates a nonrefundable earned income tax credit equivalent to 5% of the federal earned income credit, provides for yearly indexation of standard deductions, and provides for a four-year carryover of income derived from the sale or exchange of livestock sold in excess of the taxpayer's usual business practices.

Capital Gains Exemption: The program is changed from a refund program to an exemption for tax years beginning on or after January 1, 1989. 45% of net capital gains may be exempted for specific types of assets generally described as (a) real property used in a business, or from the sale of a business, in which the taxpayer materially participated, or was employed, and which was held for a minimum of 10 years, or (b) from the sale of livestock by taxpayers deriving more than half of their income from farming or ranching, or (c) from the sale of timber meeting certain I.R.S. guidelines.

Assumptions--Capital Gains

1. 1987 capital gains activity is assumed to be predictive for future years.
2. The Department was not able to specifically estimate the effects for eligible real estate and intangibles capital gains without making several relatively arbitrary assumptions which follow:
  - A. For real estate capital gains, it was assumed that 50% of real estate gains would be eligible.
  - B. For intangibles (stocks, bonds), it was assumed that 10% of intangibles would qualify.

Fiscal Effect--Capital Gains

Using the above assumptions, Departmental estimates indicate that a 45% capital gains exemption for gains for eligible real property, intangibles, and livestock would result in roughly \$6.2 to \$8.1 million in tax benefit. This impact will be increased by an unknown amount for eligible timber assets. This provision is effective for tax year 1989. The reduction to the General Fund would first occur in FY 1990.

Standard Deduction Indexation: This amendment would index standard deductions yearly effective for tax years beginning on or after January 1, 1990. Standard deductions would be indexed by 50% of the gross national product implicit price deflator but would not be subject to a trigger based on the size of the General Fund ending balance.

Assumptions--Standard Deduction Indexation, Tax Year 1990

-2-

1. Based on information from Data Resources, Incorporated, the standard deduction inflation factor for tax year 1990 is estimated to be 2.3%.
2. Increasing the current amounts of \$1,230 for individuals and \$3,030 for joint filers by 2.3% raises standard deduction amounts to \$1,260 for individuals and \$3,100 for joint filers.

Fiscal Effect--Standard Deduction Indexation, Tax Year 1990

The tax model indicates these amounts would reduce taxpayer liability by about \$1.6 million. Assuming the Department does not change withholding tables for tax year 1990, the reduction in the General Fund should first occur in FY 1991.

Earned Income Credit: A nonrefundable tax credit equivalent to 5% of the taxpayer's federal earned income tax credit is allowed for tax years beginning on or after January 1, 1990. This is estimated by the Department to reduce taxpayer liability by \$1.5 million. Assuming the Department does not change for tax year 1990, the reduction to the General Fund should first occur in FY 1991.

(LSB 2721sv.4, PDD)

FILED MAY 6, 1989

BY DENNIS PROUTY, FISCAL DIRECTOR

SENATE AMENDMENT TO HOUSE AMENDMENT TO SENATE FILE 537  
H-4497

1 Amend the House amendment, S-4106, to Senate File  
2 537, as amended, passed, and reprinted by the Senate,  
3 as follows:

4 1. By striking page 1, line 5, through page 2,  
5 line 31, and inserting the following:

6 "Sec. 300. Section 422.4, Code 1989, is amended by  
7 adding the following new subsection:

8 NEW SUBSECTION. 18. a. "Annual standard  
9 deduction factor" means an index, expressed as a  
10 percentage, determined by the department by October 15  
11 of the calendar year preceding the calendar year for  
12 which the factor is determined, which reflects the  
13 purchasing power of the dollar as a result of  
14 inflation during the fiscal year ending in the  
15 calendar year preceding the calendar year for which  
16 the factor is determined. In determining the annual  
17 standard deduction factor, the department shall use  
18 the annual percent change, but not less than zero  
19 percent, in the implicit price deflator for the gross  
20 national product computed for the second quarter of  
21 the calendar year by the bureau of economic analysis  
22 of the United States department of commerce and shall  
23 add one-half of that percent change to one hundred  
24 percent. The annual standard deduction factor and the  
25 cumulative standard deduction factor shall each be  
26 expressed as a percentage rounded to the nearest one-  
27 tenth of one percent. The annual standard deduction  
28 factor shall not be less than one hundred percent.

29 b. "Cumulative standard deduction factor" means  
30 the product of the annual standard deduction factor  
31 for the 1989 calendar year and all annual standard  
32 deduction factors for subsequent calendar years as  
33 determined pursuant to this subsection. The  
34 cumulative standard deduction factor applies to all  
35 tax years beginning on or after January 1 of the  
36 calendar year for which the latest annual standard  
37 deduction factor has been determined.

38 c. The annual standard deduction factor for the  
39 1989 calendar year is one hundred percent.

40 Sec. 400. Section 422.5, subsection 1, paragraph  
41 k, unnumbered paragraph 2, Code 1989, is amended to  
42 read as follows:

43 The state alternative minimum taxable income of a  
44 taxpayer is equal to the taxpayer's state taxable  
45 income, as computed with the deductions in section  
46 422.9, ~~except-for-the-net-capital-gain-deduction~~, with  
47 the following adjustments:

48 Sec. 401. Section 422.5, Code 1989, is amended by  
49 adding the following new subsection:

50 NEW SUBSECTION. 10. In the case of income derived

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1 from the sale or exchange of livestock which qualifies  
2 under section 451(e) of the Internal Revenue Code  
3 because of drought, the taxpayer may elect to include  
4 the income in the taxpayer's net income in the tax  
5 year following the year of the sale or exchange in  
6 accordance with rules prescribed by the director.

7 Sec. 402. Section 422.7, Code 1989, is amended by  
8 adding the following new subsection:

9 "NEW SUBSECTION. 19. Subtract forty-five percent  
10 of the net capital gain from the following:".

11 2. Page 3, by inserting before line 30 the  
12 following:

13 "Sec. 403. Section 422.9, subsection 6, Code 1989,  
14 is amended by striking the subsection.

15 Sec. 301. NEW SECTION. 422.12B EARNED INCOME TAX  
16 CREDIT.

17 1. The taxes imposed under this division, less  
18 credits allowed under sections 422.10 through 422.12,  
19 shall be reduced by an earned income credit equal to  
20 five percent of the federal earned income credit  
21 received by the taxpayer under section 32(b) of the  
22 Internal Revenue Code. Any credit in excess of the  
23 tax liability is nonrefundable.

24 2. Married taxpayers electing to file separate  
25 returns or filing separately on a combined return may  
26 avail themselves of the earned income credit by  
27 allocating the earned income credit to each spouse in  
28 the proportion that each spouse's respective earned  
29 income bears to the total combined earned income.  
30 Taxpayers affected by the allocation provisions of  
31 section 422.8 shall be permitted a deduction for the  
32 credit only in the amount fairly and equitably  
33 allocable to Iowa under rules prescribed by the  
34 director."

35 3. By striking page 3, line 43 through page 4,  
36 line 20, and inserting the following: "the 1990  
37 calendar year and each subsequent calendar year the  
38 annual and cumulative standard deduction factors to be  
39 applied to tax years beginning on or after January 1  
40 of that calendar year. The director shall compute the  
41 new dollar amounts of the standard deductions  
42 specified in section 422.9, subsection 1, by the  
43 latest cumulative standard deduction factor and round  
44 off the result to the nearest ten dollars. The annual  
45 and cumulative standard deduction factors determined  
46 by the director are not rules as defined in section  
47 17A.2, subsection 7.

48 Sec. 404. Section 422.21, unnumbered paragraph 6,  
49 Code 1989, is amended by striking the unnumbered  
50 paragraph.

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1 Sec. \_\_\_\_ . Sections 300, 301, and 104 of this Act  
2 apply to tax years beginning on or after January 1,  
3 1990.

4 Sec. \_\_\_\_ . Sections 400, 401, 402, 403, and 404 of  
5 this Act apply to tax years beginning on or after  
6 January 1, 1990.

7 4. Page 4, line 23, by striking the words "tax  
8 brackets and".

9 5. Page 4, lines 24 and 25, by striking the words  
10 ", increasing the amount of the standard deduction"  
11 and inserting the following: "providing an earned  
12 income tax credit".

RECEIVED FROM THE SENATE

H-4497 FILED MAY 7, 1989

CONCURRED (p. 2790)

SENATE FILE 537

AN ACT

RELATING TO THE INDEXING OF THE STANDARD DEDUCTION FOR INCOME TAX PURPOSES, PROVIDING AN EARNED INCOME TAX CREDIT, RELATING TO STATE INDIVIDUAL INCOME TAX BY GIVING CAPITAL GAIN DEDUCTION TREATMENT TO LIMITED AMOUNTS OF CAPITAL GAIN, AND PROVIDING CERTAIN APPLICABILITY DATES.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF IOWA:

Section 1. Section 422.4, Code 1989, is amended by adding the following new subsection:

NEW SUBSECTION. 18. a. "Annual standard deduction factor" means an index, expressed as a percentage, determined by the department by October 15 of the calendar year preceding the calendar year for which the factor is determined, which reflects the purchasing power of the dollar as a result of inflation during the fiscal year ending in the calendar year preceding the calendar year for which the factor is determined. In determining the annual standard deduction factor, the department shall use the annual percent change, but not less than zero percent, in the implicit price deflator for the gross national product computed for the second quarter of the calendar year by the bureau of economic analysis of the United States department of commerce and shall add one-half of that percent change to one hundred percent. The annual standard deduction factor and the cumulative standard deduction factor shall each be expressed as a percentage rounded to the nearest one-tenth of one percent. The annual standard deduction factor shall not be less than one hundred percent.

b. "Cumulative standard deduction factor" means the product of the annual standard deduction factor for the 1989 calendar year and all annual standard deduction factors for

subsequent calendar years as determined pursuant to this subsection. The cumulative standard deduction factor applies to all tax years beginning on or after January 1 of the calendar year for which the latest annual standard deduction factor has been determined.

c. The annual standard deduction factor for the 1989 calendar year is one hundred percent.

Sec. 2. Section 422.5, subsection 1, paragraph k, unnumbered paragraph 2, Code 1989, is amended to read as follows:

The state alternative minimum taxable income of a taxpayer is equal to the taxpayer's state taxable income, as computed with the deductions in section 422.9, ~~except for the net capital gain deduction~~, with the following adjustments:

Sec. 3. Section 422.5, Code 1989, is amended by adding the following new subsection:

NEW SUBSECTION. 10. In the case of income derived from the sale or exchange of livestock which qualifies under section 451(e) of the Internal Revenue Code because of drought, the taxpayer may elect to include the income in the taxpayer's net income in the tax year following the year of the sale or exchange in accordance with rules prescribed by the director.

Sec. 4. Section 422.7, Code 1989, is amended by adding the following new subsection:

NEW SUBSECTION. 19. Subtract forty-five percent of the net capital gain from the following:

a. Net capital gain from the sale of real property used in a business, in which the taxpayer materially participated for ten years, as defined in section 469(h) of the Internal Revenue Code, and which has been held for a minimum of ten years, or from the sale of a business, as defined in section 422.42, in which the taxpayer was employed or in which the taxpayer materially participated for ten years, as defined in section 469(h) of the Internal Revenue Code, and which has

been held for a minimum of ten years. The sale of a business means the sale of all or substantially all of the tangible personal property or service of the business.

b. Net capital gain from the sale of cattle or horses held by the taxpayer for breeding, draft, dairy, or sporting purposes for a period of twenty-four months or more from the date of acquisition; but only if the taxpayer received more than one-half of the taxpayer's gross income from farming or ranching operations during the tax year.

c. Net capital gain from the sale of breeding livestock, other than cattle or horses, if the livestock is held by the taxpayer for a period of twelve months or more from the date of acquisition; but only if the taxpayer received more than one-half of the taxpayer's gross income from farming or ranching operations during the tax year.

d. Net capital gain from the sale of timber as defined in section 631(a) of the Internal Revenue Code.

The net capital gain of paragraphs "a", "b", "c", and "d" together shall not exceed seventeen thousand five hundred dollars for the tax year. Married taxpayers who elect separate filing on a combined return for state tax purposes are treated as one taxpayer and the amount of net capital gain to be used to determine the total amount to be subtracted by them shall not exceed seventeen thousand five hundred dollars in the aggregate. Married taxpayers who file jointly or separately on a combined return shall prorate the seventeen thousand five hundred dollar limitation between them based on the ratio of each spouse's net capital gain to the total net capital gain of both spouses. In the case of married taxpayers filing separate returns, the amount of net capital gain to be used to determine the amount to be subtracted by each spouse shall not exceed eight thousand seven hundred fifty dollars.

Sec. 5. Section 422.9, subsection 6, Code 1989, is amended by striking the subsection.

Sec. 6. NEW SECTION. 422.12B EARNED INCOME TAX CREDIT.

1. The taxes imposed under this division, less credits allowed under sections 422.10 through 422.12, shall be reduced by an earned income credit equal to five percent of the federal earned income credit received by the taxpayer under section 32(b) of the Internal Revenue Code. Any credit in excess of the tax liability is nonrefundable.

2. Married taxpayers electing to file separate returns or filing separately on a combined return may avail themselves of the earned income credit by allocating the earned income credit to each spouse in the proportion that each spouse's respective earned income bears to the total combined earned income. Taxpayers affected by the allocation provisions of section 422.8 shall be permitted a deduction for the credit only in the amount fairly and equitably allocable to Iowa under rules prescribed by the director.

Sec. 7. Section 422.21, unnumbered paragraph 4, Code 1989, is amended to read as follows:

The director shall determine for the 1989 and each subsequent calendar year the annual and cumulative inflation factors for each calendar year to be applied to tax years beginning on or after January 1 of that calendar year. The director shall compute the new dollar amounts as specified to be adjusted in section 422.5 by the latest cumulative inflation factor and round off the result to the nearest one dollar. The annual and cumulative inflation factors determined by the director are not rules as defined in section 17A.2, subsection 7. The director shall determine for the 1990 calendar year and each subsequent calendar year the annual and cumulative standard deduction factors to be applied to tax years beginning on or after January 1 of that calendar year. The director shall compute the new dollar amounts of the standard deductions specified in section 422.9, subsection 1, by the latest cumulative standard deduction factor and round off the result to the nearest ten dollars. The annual and cumulative standard deduction factors determined by the

director are not rules as defined in section 17A.2, subsection 7.

Sec. 8. Section 422.21, unnumbered paragraph 6, Code 1989, is amended by striking the unnumbered paragraph.

Sec. 9. Sections 1, 6, and 7 of this Act apply to tax years beginning on or after January 1, 1990.

Sec. 10. Sections 2, 3, 4, 5, and 8 of this Act apply to tax years beginning on or after January 1, 1990.

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JO ANN ZIMMERMAN  
President of the Senate

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DONALD D. AVENSON  
Speaker of the House

I hereby certify that this bill originated in the Senate and is known as Senate File 537, Seventy-third General Assembly.

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JOHN F. DWYER  
Secretary of the Senate

Approved May 31, 1989

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TERRY E. BRANSTAD  
Governor