

## REVENUE DEPARTMENT[701]

### Regulatory Analysis

Notice of Intended Action to be published: 701—Chapter 603  
“Allocation and Apportionment”

Iowa Code section(s) or chapter(s) authorizing rulemaking: 421.14 and 422.63

State or federal law(s) implemented by the rulemaking: Iowa Code sections 422.33, 422.60 and 422.63

### *Public Hearing*

A public hearing at which persons may present their views orally or in writing will be held as follows:

November 18, 2026  
9 to 10 a.m.

Via videoconference call:  
[meet.google.com/sbm-ihix-ere](https://meet.google.com/sbm-ihix-ere)

### *Public Comment*

Any interested person may submit written or oral comments concerning this Regulatory Analysis, which must be received by the Department of Revenue no later than 4:30 p.m. on the date of the public hearing. Comments should be directed to:

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### *Purpose and Summary*

The purpose of this proposed rulemaking is to rescind and readopt Chapter 603. Chapter 603 currently provides rules related to assessments, refunds, and appeals. These rules are not unique to franchise tax and are largely duplicative of rules that exist for both individual and corporate income taxes. Therefore, the rules that exist in this chapter are proposed to be rescinded, and the content will be consolidated into 701—Chapter 300, which is applicable to all three tax types, in a concurrent rulemaking (**RA 26-363**, IAB 10/28/26).

The Department proposes to move rules related to multistate financial institutions apportioning their income within and without Iowa from 701—Chapter 602 to Chapter 603 to make them easier to find and to separate them from rules related to net income adjustment. Iowa Code section 422.33 provides a statutory method for apportioning certain categories of income, but specifically delegates to the Department the authority to set apportionment methods for categories not covered in the statute by rule. Proposed Chapter 603 provides allocation and apportionment methods for various common categories of financial institution income. They are substantially different from those in 701—Chapter 503, which is applicable to corporate income tax apportionment, since there are certain categories of income more common to financial institutions than to other businesses. The chapter also provides definitions, examples, and other useful information not included in the Iowa Code for the various apportionment methods covered in both the statute and the rules. The chapter also cross-references

rule 701—503.9(422), which provides a process by which taxpayers can request an alternative method of apportionment if they feel the method in the statute or the rules results in a disproportionate amount of their income being taxed by Iowa. This process is authorized by statute and likely constitutionally required, and the rule provides a fair and uniform process to all taxpayers seeking this type of relief.

### *Analysis of Impact*

#### **1. Persons affected by the proposed rulemaking:**

- **Classes of persons that will bear the costs of the proposed rulemaking:**

There are no known or ascertainable costs to the public associated with the apportionment rules. Apportionment of income for multistate businesses is statutorily and constitutionally required, and the Iowa Code delegates setting the specific method of apportionment for many categories of income to the Department. There may be other conceivable methods of apportionment that would result in higher or lower costs as applied to specific taxpayers, but the methods outlined in the rules have been in place for decades and have provided uniform and consistent methods of apportionment for Iowa purposes for all of that time. Rule 701—503.9(422) (cross-referenced in this chapter) does create a process for taxpayers to request permission to use an alternative method of apportionment.

- **Classes of persons that will benefit from the proposed rulemaking:**

Taxpayers, tax preparers and Department staff will benefit from the proposed rulemaking.

#### **2. Impact of the proposed rulemaking, economic or otherwise, including the nature and amount of all the different kinds of costs that would be incurred:**

- **Quantitative description of impact:**

There is no economic impact of the proposed rulemaking beyond what is contained in the underlying statutes.

- **Qualitative description of impact:**

The rules provide guidance on how to calculate the portion of a franchise taxpayer's income allocated or apportioned to Iowa and incorporate by cross-reference a method for requesting to use an alternative apportionment method if the method provided in the rules disproportionately attributes income within and without Iowa. Taxpayers wishing to use an alternative method of apportionment will likely incur some costs to complete this process, but the director's permission to use an alternative method is required by law, and the process provided by the rule ensures a uniform experience among taxpayers making these requests.

#### **3. Costs to the State:**

- **Implementation and enforcement costs borne by the agency or any other agency:**

The rules themselves impose no additional costs on the agency; they only clarify items relating to allocation and apportionment that the Department is already required by law to administer. The rules have no known impact on any other agency.

- **Anticipated effect on State revenues:**

This rulemaking implements the same apportionment methods for franchise taxpayers that have been in place for decades. The rules will be the same for these taxpayers both before and after the rulemaking, so no effect on State revenues is anticipated.

#### **4. Comparison of the costs and benefits of the proposed rulemaking to the costs and benefits of inaction:**

The Iowa Code provides a statutory method for determining how certain specific categories of income should be attributed within and without the State, but also delegates to the Department the authority to set allocation and apportionment methods for categories of income not explicitly covered by the statute. Without these rules, there would be no Iowa apportionment method for various types of income not explicitly listed in the statute.

#### **5. Determination whether less costly methods or less intrusive methods exist for achieving the purpose of the proposed rulemaking:**

There are no known less costly or intrusive methods.

**6. Alternative methods considered by the agency:**

• **Description of any alternative methods that were seriously considered by the agency:**

Since the Iowa Code delegates setting apportionment methods for some categories of income to the Department, the only alternative would be to simply not provide an Iowa apportionment method for those categories of income.

• **Reasons why alternative methods were rejected in favor of the proposed rulemaking:**

Not providing some of these rules would leave taxpayers with no clear method of apportioning certain common types of income within and without Iowa, making it difficult or impossible for multistate financial institutions to file fair and accurate Iowa franchise returns.

*Small Business Impact*

**If the rulemaking will have a substantial impact on small business, include a discussion of whether it would be feasible and practicable to do any of the following to reduce the impact of the rulemaking on small business:**

- Establish less stringent compliance or reporting requirements in the rulemaking for small business.
- Establish less stringent schedules or deadlines in the rulemaking for compliance or reporting requirements for small business.
- Consolidate or simplify the rulemaking's compliance or reporting requirements for small business.
- Establish performance standards to replace design or operational standards in the rulemaking for small business.
- Exempt small business from any or all requirements of the rulemaking.

**If legal and feasible, how does the rulemaking use a method discussed above to reduce the substantial impact on small business?**

The allocation and apportionment methods associated with these rules are either imposed by the Iowa Code or delegated by the Iowa Code to the Department to create by rule. Allocation and apportionment of income subject to State tax is constitutionally required. Not apportioning income would typically be disadvantageous to any multistate business, regardless of size, since it would likely result in double taxation across states. The rules do provide a process by which any business could seek an alternative method of apportionment, and a small business that was somehow uniquely affected by these rules would be entitled to utilize this process to seek an alternative method.

*Text of Proposed Rulemaking*

ITEM 1. Rescind 701—Chapter 603 and adopt the following new chapter in lieu thereof:

CHAPTER 603  
ALLOCATION AND APPORTIONMENT

**701—603.1(422) Basis of franchise tax.** Iowa Code section 422.60 imposes a franchise tax on financial institutions as defined in Iowa Code section 422.61 for the privilege of doing business within the state. The tax is measured by net income. For financial institutions subject to the tax, the tax is levied and collected only on income that may accrue or be recognized to the financial institutions from business done or carried on in the state plus net income from certain sources without the state that by rule follows the commercial domicile of the financial institution.

If a financial institution carries on business entirely within the state of Iowa, no allocation or apportionment of its income may be made. The financial institution will be presumed to be carrying on its business entirely within the state of Iowa if its activities are carried on only within Iowa, even

though it receives income from sources outside the state in the form of interest, dividends, royalties, and other sources of income from intangibles.

**603.1(1) Definition—doing business.** The term “doing business” is used in a comprehensive sense and includes all activities or any transactions for the purpose of financial or pecuniary gain or profit. Irrespective of the nature of its activities, every financial institution organized for profit and carrying out any of the purposes of its organization shall be deemed to be “doing business.” In determining whether a financial institution is doing business, it is immaterial whether its activities actually result in a profit or loss.

**603.1(2) Definition—carrying on business partly within and partly without the state.** “Carrying on business partly within and partly without the state” means having business activities in at least one other state sufficient to meet the minimum constitutional standards for doing business in a state under the due process and commerce clauses of the United States Constitution.

*a. Annual determination.* The determination of whether a financial institution is carrying on business partly within and partly without the state must be made on a tax-year-by-tax-year basis. The activities of past or future years have no bearing on the current year.

*b. Activities that qualify as doing business.* The following nonexclusive activities if done on a regular and continuing basis by financial institution officers or employees in at least one other state would constitute the minimum activities that would meet the constitutional standards for doing business in a state under the due process and commerce clauses of the United States Constitution:

- (1) Solicitation of loans by traveling loan officers.
- (2) Collection of overdue accounts.
- (3) Any other activities carried on in advancement, promotion, or fulfillment of the business of the financial institution.

This rule is intended to implement Iowa Code sections 422.60 and 422.63.

#### **701—603.2(422) Allocation and apportionment.**

**603.2(1)** The classification of income by the labels customarily given, such as interest, dividends, rents, and royalties, is of no aid in determining whether that income is business or nonbusiness income. Interest, dividends, rents and royalties shall be apportioned as business income to the extent the income was earned as a part of a financial institution’s unitary business, a portion of which is conducted in Iowa. Whether income is part of a financial institution’s unitary business income depends upon the facts and circumstances in the particular situation. The burden of proof is upon the taxpayer to show that the treatment of income on the return as filed is proper. There is a rebuttable presumption that an affiliated group of financial institutions in the same line of business have a unitary relationship, although that is not the only element used in determining unitariness.

**603.2(2)** Application of related expense to nonbusiness income. Subrule 603.2(1) deals with the separation of net income; therefore, determination and application of directly related expenses must be made before allocation and apportionment within and without Iowa.

*a. Directly related expenses.* A directly related expense is an expense that can be specifically attributed to an item of income. Interest expense is considered directly related to a specific property that generates, has generated, or could reasonably have been expected to generate gross income if the existence of all of the facts and circumstances described below are established.

- (1) The indebtedness on which the interest was paid was specifically incurred for the purpose of purchasing, maintaining, or improving the specific property;
- (2) The proceeds of the borrowing were actually applied to the specified purpose;
- (3) The creditor can look only to the specific property (or any lease or other interest therein) as security for the loan;
- (4) It may be reasonably assumed that the return on or from the property will be sufficient to fulfill the terms and conditions of the loan agreement with respect to the amount and timing of payment of principal and interest; and

(5) There are restrictions in the loan agreement on the disposal or use of the property consistent with the assumptions described in subparagraphs 603.2(2)“a”(3) and “a”(4).

*b. Expenses not considered directly related.* A deduction for interest cannot be considered definitely related solely to specific property, even though the above facts and circumstances are present in form, if any of the facts and circumstances are not present in substance. Any expense directly attributable to allocable interest, dividends, rents and royalties shall be deducted from income to arrive at net allocable income.

EXAMPLE: For purposes of this example, it is assumed that the taxpayer has nonbusiness rental income. The taxpayer invests in a 20-story office building. Under the terms of the lease agreements, the taxpayer provides heat, electricity, janitorial services, and maintenance. The taxpayer also pays the property taxes. Construction of the building was funded through borrowings that meet the criteria of a direct expense under the provisions of this paragraph. The directly related expenses to the operation of the property are:

|                     |                    |
|---------------------|--------------------|
| Interest expense    | \$1,200,000        |
| Property taxes      | 500,000            |
| Depreciation        | 500,000            |
| Electricity         | 300,000            |
| Heat                | 200,000            |
| Insurance           | 150,000            |
| Janitorial services | 100,000            |
| Repairs             | 50,000             |
| Total expenses      | <u>\$3,000,000</u> |

The directly related expense of the allocable rental income is \$3,000,000.

This rule is intended to implement Iowa Code section 422.63.

**701—603.3(422) Net gains and losses from the sale of assets.** For purposes of administration of this rule, a capital gain or loss means the sale price or value at the time of disposal of an asset less the adjusted basis, whether reportable as short-term or long-term capital gain or ordinary income for federal income tax purposes.

**603.3(1) Apportionment of business gains.** Gain or loss from the sale, exchange, or other disposition of real or tangible or intangible personal property, if the property while owned by the taxpayer was used in the taxpayer’s trade or business, shall be apportioned by the business activity ratio applicable to the year the gain or loss is reported on the federal income tax return and may at the taxpayer’s election be included in the computation of the business activity ratio as follows:

*a.* Gain from the sale, exchange, or other disposition of real property shall be included in the numerator if the property is located in Iowa.

*b.* Gain from the sale, exchange, or other disposition of tangible personal property shall be included in the numerator if:

(1) The property has a situs in Iowa at the time of sale; or

(2) The taxpayer’s commercial domicile is in Iowa and the taxpayer is not taxable in the state in which the property had a situs.

*c.* Gains from the sale, exchange, or other disposition of intangible personal property shall be included in the numerator if the taxpayer’s commercial domicile is in Iowa.

*d.* All gains shall be included in the denominator of the business activity ratio.

A taxpayer cannot elect to exclude or include gains or loss from the sale of assets where the election would result in an understatement of income reasonably attributable to Iowa. Noninclusive examples of gains or loss from the sale, exchange or other disposition of real or tangible or intangible property that cannot be included in the computation of the business activity ratio because to do

so would result in an understatement of net income reasonably attributable to Iowa are the gain recognized under an election pursuant to Section 338 of the Internal Revenue Code or gain recognized under Section 631(a) of the Internal Revenue Code.

**603.3(2) Allocation of nonbusiness gains.** Gain or loss from the sale, exchange, or other disposition of property not used in the taxpayer's trade or business shall be allocated as follows:

*a.* Gains or losses from the sale, exchange, or other disposition of real property located in Iowa are allocable to Iowa.

*b.* Gains or losses from the sale, exchange, or other disposition of tangible personal property are allocable to Iowa if:

(1) The property has a situs in Iowa at the time of sale; or

(2) The taxpayer's commercial domicile is in Iowa and the taxpayer is not taxable in the state in which the property had a situs.

*c.* Gains or losses from the sale, exchange, or other disposition of intangible personal property are allocable to Iowa if the taxpayer's commercial domicile is in Iowa.

This rule is intended to implement Iowa Code section 422.63.

**701—603.4(422) Apportionment factor.** In determining the total net taxable income, the apportionable income attributable to Iowa, as determined by use of the apportionment fraction, is added to the nonapportionable income allocable to Iowa.

**603.4(1)** Receipts derived from transactions and activities in the regular course of trade or business that produce business income are included in the denominator of the apportionment factor. Income that is not subject to the Iowa franchise tax shall not be included in the computation of the apportionment factor.

**603.4(2)** The numerator of the apportionment factor is that portion of the total receipts included in the denominator of the taxpayer attributable to Iowa during the income year determined as follows:

*a.* Receipts from the lease, rental, or other use of real property are included in the numerator if the real property is located in Iowa.

*b.* Receipts from the sale of tangible personal property are included in the numerator if the property is delivered or shipped to a purchaser in Iowa regardless of the f.o.b. point or other conditions of the sales.

*c.* Receipts from the use of tangible personal property are included in the numerator of the business activity formula to the extent that property is utilized in Iowa. The extent of utilization of tangible personal property in a state is determined by multiplying the rent by a fraction, the numerator of which is the number of days of physical location of the property in the state during the rental period in the taxable year and the denominator of which is the number of days of physical location of the property everywhere during all rental periods in the taxable year. If the physical location of the property during the rental period is unknown or not ascertainable by the taxpayer, tangible personal property is utilized in the state in which the property was located at the time the rental payer obtained possession.

*d.* All royalty income from intangible personal property determined to be business income is included in the numerator of the business activity formula if the taxpayer's commercial domicile is in Iowa.

*e.* All royalty income from tangible personal property or real property determined to be business income is included in the numerator of the business activity formula if the situs of the tangible personal property or real property is within Iowa.

*f.* Interest and other receipts from assets in the nature of loans (including federal funds sold and banker's acceptances) and installment obligations are attributed to the state where the borrower is located.

*g.* Interest income from a participating bank's portion of participation loan is attributed to the state where the borrower is located.

*h.* Interest income from loans solicited by traveling loan officers is attributed to the state where the borrower is located.

*i.* Interest or service charges from bank, travel, and entertainment credit card receivables and credit card holders' fees are attributed to the state in which the credit card holder resides in the case of an individual or, if a corporation, to the state of the corporation's commercial domicile.

*j.* Merchant discount income derived from bank and financial corporation credit card holder transactions with a merchant is attributed to the state in which the merchant is located. It is presumed that the location of the merchant is the address on the invoice submitted by the merchant to the taxpayer.

*k.* Receipts for the performance of fiduciary services are attributable to the state where the services are principally performed.

*l.* Receipts from investments of a bank in securities, the income from which constitutes business income, are attributed to its commercial domicile except that:

(1) Receipts from securities used to maintain reserves against deposits to meet federal and state reserve deposit requirements are attributed to each state based upon the ratio that total deposits in the state bear to total deposits everywhere.

(2) Receipts from securities owned by a bank but held by a state treasurer or other public official or pledged to secure public or trust funds deposited in the bank are attributed to the banking office at which the secured deposit is maintained.

*m.* Receipts (fees or charges) from the issuance of traveler's checks and money orders are attributed to the state where the taxpayer's office is located that issued the traveler's checks. If the traveler's checks are issued by an independent representative or agent of the taxpayer, the fees or charges shall be attributed to the state where the independent representative or agent issued the traveler's checks.

*n.* Fees, commissions, or other compensation for financial services rendered for a customer located in Iowa or an account maintained within Iowa are attributed to Iowa.

*o.* Any other gross receipts resulting from the operation as a financial organization within Iowa are attributed to Iowa to the extent the items do not represent a recapture of an expense.

*p.* Receipts from management services if the recipient of the management services is located in Iowa are attributed to Iowa.

This rule is intended to implement Iowa Code section 422.63.

**701—603.5(422) Allocation and apportionment of income in special cases.** If a taxpayer feels that the allocation and apportionment method as prescribed by rule 701—603.4(422) in the taxpayer's case results in an injustice, the taxpayer may petition the department for permission to determine the taxable net income, both allocable and apportionable, to the state on some other basis as provided in rule 701—503.9(422).

This rule is intended to implement Iowa Code section 422.63.