

**701—403.3(422) Distributions.** Distributions from income not previously taxed by Iowa include the amount of all cash distributions and the fair market value of all property distributions made during the year, except as follows:

1. Distributions from income not subject to Iowa tax due to exclusion under Iowa Code section 422.7 (i.e., interest from federal securities or certain securities issued by Iowa). For purposes hereof, all distributions for a year shall be deemed to be made proportionally from income subject to Iowa tax and from income not subject to Iowa tax. Distributions from income apportioned outside of Iowa shall not be deemed to be made from income not subject to Iowa tax.

2. Distributions from income previously taxed by Iowa for a year in which the S corporation was a C corporation and which is taxed as a dividend or capital gain for federal income tax purposes.

3. Distributions from income previously taxed by Iowa for a year prior to the first tax year the resident shareholder elected to apportion income within and without Iowa.

4. Distributions treated as a return of capital for federal income tax purposes for tax years beginning prior to January 1, 2004.

5. For tax years beginning on or after January 1, 2004, any distributions paid from income for which the taxpayer can prove that Iowa tax has been previously paid. Any distributions paid from income apportioned outside of Iowa for tax years in which the resident shareholder elected to apportion income within and without Iowa will be considered distributions for which Iowa tax has not been previously paid, and cannot be excluded for purposes of this rule.

For purposes of this rule, a distribution is taken into account on the date the corporation makes the distribution, regardless of when the distribution is treated as received by the shareholder. Distributions shall first be deemed made from current year income of the S corporation to the extent thereof. If distributions during a year exceed the current income of the S corporation, any excess distributions shall be considered made first from the immediately preceding year income of the S corporation, and then to each preceding year income of the S corporation in reverse chronological order, and then in accordance with the ordering rules set forth in Section 1368 of the Internal Revenue Code and the regulations thereunder.

EXAMPLE: An S corporation earned income of \$20,000 in 2002, income of \$30,000 in 2003 and income of \$40,000 in 2004. The S corporation made no distributions during 2002 and 2003 and made distributions of \$75,000 during 2004. The distributions will come first from the \$40,000 income earned in 2004. The excess distributions of \$35,000 will come first from the \$30,000 income earned during 2003, and the remaining \$5,000 will come from the income earned during 2002.

This rule is intended to implement Iowa Code section 422.8, subsection 2.  
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