

701—502.12(422) Federal income tax deduction. “Federal income taxes” shall mean those income taxes paid or payable to the United States Government and shall not include taxes paid or payable or taxes deemed to have been paid to a foreign country. *Construction Products, Inc. v. Briggs, State Board of Tax Review*, Case No. 25, February 1, 1972. “Federal income taxes” includes the federal alternative minimum tax. For tax years beginning on or after January 1, 1990, and before January 1, 1996, “federal income taxes” includes the federal environmental tax. Because the federal environmental tax is deducted in computing federal taxable income and Iowa Code subsection 422.35(4) only allows a deduction for 50 percent of the federal income tax paid or accrued, the federal environmental tax deducted in computing federal taxable income must be added to federal taxable income.

502.12(1) Cash basis taxpayer.

a. When a taxpayer is reporting on the cash basis, 50 percent of the amount of federal income taxes actually paid during the taxable period is allowable as a deduction, whether or not such taxes represent the preceding year’s tax or additional taxes for prior years. Fifty percent of a federal tax refund shall be reported as income in the year received.

b. A corporation reporting on the cash basis may deduct 50 percent of the federal income tax on the accrual basis if an election is made upon filing the first return. If the corporation claims an accrual deduction on the first return, it shall be considered as an election. Once the election is made, the corporation may change the basis of federal income tax deduction only with the permission of the director. If a change in accounting method is approved or required by the Internal Revenue Service, the director is deemed to have approved the change in the basis of the federal tax deduction.

c. The federal income tax deduction during the transitional period following a change in accounting method from cash to accrual is the accrual deduction in the year of change, plus any cash payment of federal income tax paid in the year of the change for the tax year prior to the change in accounting method, reduced by a refund of federal income tax paid for the tax year prior to the year of the change in accounting method received in the year of the change. For the year of change and years subsequent to the year of the change, the deduction shall be the accrual deduction plus any federal income tax paid for a tax year prior to the year of change as a result of an amended federal return or federal audit, reduced by any refund of federal income tax paid for a tax year prior to the year of the change in accounting method.

d. The federal income tax deduction during the transitional period following a change in accounting method from accrual to cash is the cash deduction in the year of change, plus any cash payment of federal estimated income tax paid in the year prior to the year of the change for the year of the change. Any refund of federal income tax from a tax year prior to the year of the change received in the year of the change or in a subsequent year is properly accrued to the prior tax year. Any payment of federal income tax due to an amended return or federal audit for a tax year prior to the year of the change made in the year of the change or a subsequent year is accrued to that prior tax year. (For information on amended returns, see 701—subrule 52.3(4).)

502.12(2) Accrual basis taxpayer.

a. The amount of federal income tax to be allowed as a deduction for an accrual basis taxpayer is limited to 50 percent of the actual federal income tax liability for that year.

b. Additional federal income taxes and refunds of federal income taxes (except for 53.12(2) “c”) shall be a part of the tax liability accrued for such prior years.

c. Refunds resulting from net operating loss carrybacks, investment credit carrybacks, unused excess profits tax credits, and similar items shall be included in income for Iowa corporation income tax purposes in the year in which such refunds are legally accrued.

502.12(3) Reserved.

502.12(4) Consolidated federal income tax allocation.

a. When a corporation joins with at least one other corporation in the filing of a consolidated federal income tax return, the allowable deduction shall be 50 percent of the consolidated federal income tax liability allocable to that corporation. The allocation of the consolidated federal income tax shall be determined as follows: The net consolidated federal income tax liability is multiplied by a fraction, the numerator of which is the taxpayer’s federal taxable income as computed on a separate basis, and the

denominator of which is the total federal taxable incomes of each corporation included in the consolidated return. If the computation of the taxable income of a member results in an excess of deductions over gross income such member's taxable income shall be zero. *Sibley State Bank v. Bair, State Board of Tax Review*, Docket No. 182, May 26, 1978. *Internorth, Inc., and Northern Propane Gas Company v. Iowa State Board of Tax Review, Iowa Department of Revenue and Gerald D. Bair, Director of Revenue*, 333 N.W.2d 471 (Iowa 1983).

b. If a corporation joins with at least one other corporation in the filing of a consolidated federal income tax return, the federal income tax deduction allowed the Iowa taxpayer shall not exceed 50 percent of the consolidated federal income tax liability.

This rule is intended to implement Iowa Code section 422.35.

[Editorial change: IAC Supplement 11/2/22]