

JAN 8 1996  
WAYS AND MEANS

HOUSE FILE 2023  
BY LARSON

Passed House, Date \_\_\_\_\_ Passed Senate, Date \_\_\_\_\_  
Vote: Ayes \_\_\_\_\_ Nays \_\_\_\_\_ Vote: Ayes \_\_\_\_\_ Nays \_\_\_\_\_  
Approved \_\_\_\_\_

A BILL FOR

1 An Act relating to the computation of the tax imposed on  
2 shareholders of corporations whose income is taxed to its  
3 shareholders and providing an effective and applicability date  
4 provision.

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

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HF 2023

1 Section 1. Section 422.5, subsection 1, paragraph j, Code  
2 1995, is amended by adding the following new unnumbered  
3 paragraph:

4 NEW UNNUMBERED PARAGRAPH. The tax imposed upon the taxable  
5 income of a resident shareholder in a corporation which has in  
6 effect for the tax year an election under subchapter S of the  
7 Internal Revenue Code and carries on business within and  
8 without the state may be computed by reducing the amount  
9 determined pursuant to paragraphs "a" through "i" by the  
10 amounts of nonrefundable credits under this division and by  
11 multiplying this resulting amount by a fraction of which the  
12 resident's net income allocated to Iowa, as determined in  
13 section 422.8, subsection 2, paragraph "b", is the numerator  
14 and the resident's total net income computed under section  
15 422.7 is the denominator. This paragraph also applies to  
16 individuals who are residents of Iowa for less than the entire  
17 tax year.

18 Sec. 2. Section 422.5, subsection 1, paragraph k,  
19 unnumbered paragraph 4, Code 1995, is amended to read as  
20 follows:

21 In the case of a resident, including a resident estate or  
22 trust, the state's apportioned share of the state alternative  
23 minimum tax is one hundred percent of the state alternative  
24 minimum tax computed in this subsection. In the case of a  
25 resident or part-year resident shareholder in a corporation  
26 which has in effect for the tax year an election under  
27 subchapter S of the Internal Revenue Code and carries on  
28 business within and without the state, a nonresident,  
29 including a nonresident estate or trust, or an individual,  
30 estate, or trust that is domiciled in the state for less than  
31 the entire tax year, the state's apportioned share of the  
32 state alternative minimum tax is the amount of tax computed  
33 under this subsection, reduced by the applicable credits in  
34 sections 422.10 through 422.12 and this result multiplied by a  
35 fraction with a numerator of the sum of state net income

1 allocated to Iowa as determined in section 422.8, subsection  
2 2, paragraph "a" or "b" as applicable, plus tax preference  
3 items, adjustments, and losses under subparagraph (1)  
4 attributable to Iowa and with a denominator of the sum of  
5 total net income computed under section 422.7 plus all tax  
6 preference items, adjustments, and losses under subparagraph  
7 (1). In computing this fraction, those items excludable under  
8 subparagraph (1) shall not be used in computing the tax  
9 preference items. Married taxpayers electing to file separate  
10 returns or separately on a combined return must allocate the  
11 minimum tax computed in this subsection in the proportion that  
12 each spouse's respective preference items, adjustments, and  
13 losses under subparagraph (1) bear to the combined preference  
14 items, adjustments, and losses under subparagraph (1) of both  
15 spouses.

16 Sec. 3. Section 422.7, Code Supplement 1995, is amended by  
17 adding the following new subsection:

18 NEW SUBSECTION. 35. Resident shareholders of a  
19 corporation which has an election in effect under subchapter S  
20 of the Internal Revenue Code shall add their proportionate  
21 share of a deemed distribution of current year income, upon  
22 which Iowa income tax has not been paid as determined under  
23 rules of the director, to the extent that the salaries, wages,  
24 or other compensation for services performed by all  
25 shareholders does not equal ten percent of net income of the  
26 corporation computed in accordance with section 422.35 and  
27 considering items of income and expense which pass directly to  
28 the shareholders under provisions of the Internal Revenue Code  
29 before deduction of shareholders' salaries, wages, or other  
30 compensation for services performed. In addition there shall  
31 be added any cash or the value of any property distributions  
32 made to the extent they are made from income upon which Iowa  
33 income tax has not been paid as determined under rules of the  
34 director.

35 Sec. 4. Section 422.8, subsection 2, Code 1995, is amended

1 to read as follows:

2 2. a. Nonresident's net income allocated to Iowa is the  
3 net income, or portion thereof, which is derived from a  
4 business, trade, profession, or occupation carried on within  
5 this state or income from any property, trust, estate, or  
6 other source within Iowa. However, income derived from a  
7 business, trade, profession, or occupation carried on within  
8 this state and income from any property, trust, estate, or  
9 other source within Iowa shall not include distributions from  
10 pensions, including defined benefit or defined contribution  
11 plans, annuities, individual retirement accounts, and deferred  
12 compensation plans or any earnings attributable thereto so  
13 long as the distribution is directly related to an  
14 individual's documented retirement and received while the  
15 individual is a nonresident of this state. If a business,  
16 trade, profession, or occupation is carried on partly within  
17 and partly without the state, only the portion of the net  
18 income which is fairly and equitably attributable to that part  
19 of the business, trade, profession, or occupation carried on  
20 within the state is allocated to Iowa for purposes of section  
21 422.5, subsection 1, paragraph "j", and section 422.13 and  
22 income from any property, trust, estate, or other source  
23 partly within and partly without the state is allocated to  
24 Iowa in the same manner, except that annuities, interest on  
25 bank deposits and interest-bearing obligations, and dividends  
26 are allocated to Iowa only to the extent to which they are  
27 derived from a business, trade, profession, or occupation  
28 carried on within the state.

29 b. A resident's income allocable to Iowa is the income  
30 determined under section 422.7 reduced by the net income or  
31 loss of a corporation which is fairly and equitably  
32 attributable without the state under section 422.33. For the  
33 purposes of this paragraph, "corporation" means a corporation  
34 which has in effect for the tax year an election under  
35 subchapter S of the Internal Revenue Code and carries on

1 business partly within and partly without the state. This  
2 paragraph also applies to individuals who are residents of  
3 Iowa for less than the entire tax year.

4 Sec. 5. Section 422.8, Code 1995, is amended by adding the  
5 following new subsection:

6 NEW SUBSECTION. 6. If the resident or part-year resident  
7 is a shareholder of a corporation which has in effect an  
8 election under subchapter S of the Internal Revenue Code,  
9 subsections 1 and 3 do not apply to any income taxes paid to  
10 another state or foreign country on the income from the  
11 corporation which has in effect an election under subchapter S  
12 of the Internal Revenue Code.

13 Sec. 6. This Act takes effect upon enactment and applies  
14 retroactively to January 1, 1996, for tax years beginning on  
15 or after that date.

16 EXPLANATION

17 Under current statutory provisions, a nonresident  
18 shareholder of a subchapter S corporation computes an amount  
19 of Iowa individual income tax on the nonresident's total  
20 income earned everywhere and then that amount of tax is  
21 prorated to Iowa in the ratio of gross income from Iowa  
22 sources to total gross income.

23 The bill taxes the income from a subchapter S corporation  
24 for a resident shareholder the same way as the income is taxed  
25 for a nonresident. An amount of Iowa individual income tax is  
26 computed on the total resident shareholder's total income  
27 everywhere and then the amount of tax is prorated to Iowa in  
28 the ratio of gross income everywhere reduced by the non-Iowa  
29 income of the subchapter S corporation to total income  
30 everywhere. The resident shareholder may still take an out-  
31 of-state tax credit on income other than income from the  
32 subchapter S corporation for taxes paid to another state.

33 The bill applies retroactively to January 1, 1996, for tax  
34 years beginning on or after that date.

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