

S-3/19/97 W. & Means
S-4/10/97 No Pass

FEB 20 1997
WAYS & MEANS CALENDAR

HOUSE FILE 306
BY COMMITTEE ON WAYS AND MEANS

(SUCCESSOR TO HSB 112)

Passed House, Date 3/18/97 ^(p.669) Passed Senate, Date 4-15-97 ^{p.1181}
Vote: Ayes 88 Nays 10 Vote: Ayes 41 Nays 7
Approved May 2, 1997

A BILL FOR

1 An Act relating to the individual income tax by extending the
2 special method of computation of tax for value-added S
3 corporation shareholders to all S corporation shareholders and
4 eliminating the refund limitation and including effective and
5 retroactive applicability date provisions.

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

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HT 306

1 Section 1. Section 422.4, subsection 18, Code 1997, is
2 amended by striking the subsection.

3 Sec. 2. Section 422.5, subsection 1, paragraph j,
4 subparagraph (2), subparagraph subdivisions (a) and (c), Code
5 1997, are amended by striking the subparagraph subdivisions.

6 Sec. 3. Section 422.5, subsection 1, paragraph j,
7 subparagraph (2), Code 1997, is amended to read as follows:

8 (2) The tax imposed upon the taxable income of a resident
9 shareholder in ~~a value-added~~ an S corporation which has in
10 effect for the tax year an election under subchapter S of the
11 Internal Revenue Code and carries on business within and
12 without the state may be computed by reducing the amount
13 determined pursuant to paragraphs "a" through "i" by the
14 amounts of nonrefundable credits under this division and by
15 multiplying this resulting amount by a fraction of which the
16 resident's net income allocated to Iowa, as determined in
17 section 422.8, subsection 2, paragraph "b", is the numerator
18 and the resident's total net income computed under section
19 422.7 is the denominator. If a resident shareholder has
20 elected to take advantage of this subparagraph, and for the
21 next tax year elects not to take advantage of this
22 subparagraph, the resident shareholder shall not reelect to
23 take advantage of this subparagraph for the three tax years
24 immediately following the first tax year for which the
25 shareholder elected not to take advantage of this
26 subparagraph, unless the director consents to the reelection.
27 This paragraph subparagraph also applies to individuals who
28 are residents of Iowa for less than the entire tax year.

29 ~~(a)--In order for a resident shareholder in a value-added~~
30 ~~corporation which has in effect for the tax year an election~~
31 ~~under subchapter S of the Internal Revenue Code and carries on~~
32 ~~business within and without the state, to claim the benefits~~
33 ~~of apportionment of income of the value-added S corporation,~~
34 ~~the taxpayer must completely fill out the return, determine~~
35 ~~the taxpayer's income tax liability without the benefit of~~

1 apportionment-of-the-value-added-corporation's-income,--and-pay
2 the-amount-of-tax-owed.--The-taxpayer-shall-recompute-the
3 taxpayer's-income-tax-liability,--by-applying-the-provisions-of
4 this-subparagraph-on-a-special-return.--This-special-return
5 shall-be-filed-under-rules-of-the-director-and-constitutes-a
6 claim-for-refund-of-the-difference-between-the-amount-of-tax
7 the-taxpayer-paid-as-determined-without-the-provisions-of-this
8 subparagraph-and-the-amount-of-tax-determined-with-the
9 provisions-of-this-subparagraph:

10 (b) This subparagraph shall not affect the amount of the
11 taxpayer's checkoff to the Iowa election campaign fund under
12 section 56.18, the checkoff for the fish and game fund in
13 section 456A.16, the credits from tax provided in sections
14 422.10, 422.11A, and 422.12 and the allocation of these
15 credits between spouses if the taxpayers filed separate
16 returns or separately on combined returns.

17 (c)--For-any-tax-year,--the-aggregate-amount-of-refund
18 claims-that-shall-be-paid-pursuant-to-this-subparagraph-shall
19 not-exceed-five-million-dollars.--If,--for-a-tax-year,--the
20 aggregate-amount-of-refund-claims-filed-pursuant-to-this
21 subparagraph-exceeds-five-million-dollars,--each-claim-for
22 refund-shall-be-paid-on-a-pro-rata-basis-so-that-the-aggregate
23 amount-of-refund-claims-does-not-exceed-five-million-dollars.
24 In-the-case-where-refund-claims-are-not-paid-in-full,--the
25 amount-of-the-refund-to-which-the-taxpayer-is-entitled-under
26 this-subparagraph-is-the-pro-rata-amount-that-was-paid-and-the
27 taxpayer-is-not-entitled-to-a-refund-of-the-unpaid-portion-and
28 is-not-entitled-to-carry-that-amount-forward-or-backward-to
29 another-tax-year.--Taxpayers-shall-not-use-refunds-as
30 estimated-payments-for-the-succeeding-tax-year.--Taxpayers
31 whose-tax-years-begin-on-January-1-must-file-their-refund
32 claims-by-October-31-of-the-calendar-year-following-the-end-of
33 their-tax-year-to-be-eligible-for-refunds.--Taxpayers-whose
34 tax-years-begin-on-a-date-other-than-January-1-must-file-their
35 refund-claims-by-the-end-of-the-tenth-month-following-the-end

~~1 of their tax years to be eligible. The department shall
2 determine on February 1 of the second succeeding calendar year
3 if the total amount of claims for refund exceeds five million
4 dollars for the tax year. Notwithstanding any other
5 provision, interest shall not be due on any refund claims that
6 are paid by the last day of February of the second succeeding
7 calendar year. If the claim is not payable on February 1 of
8 the second succeeding calendar year, because the taxpayer is a
9 fiscal year filer, then the amount of the claim allowed shall
10 be in the same ratio as the refund claims available on
11 February 1 of the second succeeding calendar year. These
12 claims shall be funded by moneys appropriated for payment of
13 individual income tax refunds.~~

14 Sec. 4. Section 422.5, subsection 1, paragraph k,
15 unnumbered paragraph 4, Code 1997, is amended to read as
16 follows:

17 In the case of a resident, including a resident estate or
18 trust, the state's apportioned share of the state alternative
19 minimum tax is one hundred percent of the state alternative
20 minimum tax computed in this subsection. In the case of a
21 resident or part-year resident shareholder in a ~~value-added~~ an
22 S corporation which has in effect for the tax year an election
23 under subchapter S of the Internal Revenue Code and carries on
24 business within and without the state, a nonresident,
25 including a nonresident estate or trust, or an individual,
26 estate, or trust that is domiciled in the state for less than
27 the entire tax year, the state's apportioned share of the
28 state alternative minimum tax is the amount of tax computed
29 under this subsection, reduced by the applicable credits in
30 sections 422.10 through 422.12 and this result multiplied by a
31 fraction with a numerator of the sum of state net income
32 allocated to Iowa as determined in section 422.8, subsection
33 2, paragraph "a" or "b" as applicable, plus tax preference
34 items, adjustments, and losses under subparagraph (1)
35 attributable to Iowa and with a denominator of the sum of

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

12 Sec. 5. Section 422.8, subsection 2, paragraph b,
13 unnumbered paragraph 1, Code 1997, is amended to read as
14 follows:

15 A resident's income allocable to Iowa is the income
16 determined under section 422.7 reduced by items of income and
17 expenses from ~~a-subchapter an~~ an S corporation ~~which-is-a-value-~~
18 ~~added-corporation~~ that carries on business within and without
19 the state when those items of income and expenses pass
20 directly to the shareholders under provisions of the Internal
21 Revenue Code. These items of income and expenses are
22 increased by the greater of the following:

23 Sec. 6. Section 422.8, subsection 6, Code 1997, is amended
24 to read as follows:

25 6. If the resident or part-year resident is a shareholder
26 of ~~a-value-added~~ an S corporation which has in effect an
27 election under subchapter S of the Internal Revenue Code,
28 subsections 1 and 3 do not apply to any income taxes paid to
29 another state or foreign country on the income from the ~~value-~~
30 ~~added~~ corporation which has in effect an election under
31 subchapter S of the Internal Revenue Code.

32 Sec. 7. Section 2 of this Act applies retroactively to
33 January 1, 1997, for tax years beginning on or after that
34 date.

35 Sec. 8. This Act, except for section 2 of this Act, is

1 effective January 1, 1998, and applies to tax years beginning
2 on or after that date.

3 EXPLANATION

4 Present law allows shareholders of an S corporation which
5 is a value-added corporation to reduce its individual income
6 tax by use of a different method of computing the tax. The
7 difference between the regular method and the alternative
8 method constitutes a claim for refund of tax owed. However,
9 the aggregate amount of refunds shall not exceed \$5 million
10 per tax year.

11 This bill expands the opportunity for a reduction in tax to
12 shareholders of all S corporations regardless of whether they
13 are value-added corporations or not. This expansion is
14 effective January 1, 1998, for tax years beginning on or after
15 that date.

16 The bill also eliminates the limitation of \$5 million on
17 the aggregate amount of claims for refunds and the need to
18 file claims for refunds. This provision applies retroactively
19 to January 1, 1997, for tax years beginning on or after that
20 date.

21 The bill also provides that if a taxpayer elects to take
22 advantage of the provision to reduce the taxpayer's tax and
23 later elects not to take advantage of the tax reduction
24 provisions, then the taxpayer cannot reelect to take advantage
25 of the tax reduction provisions for the next three tax years
26 unless permitted by the director of revenue and finance. This
27 provision takes effect January 1, 1998, and applies to tax
28 years beginning on or after that date.

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**HOUSE FILE 306
FISCAL NOTE**

A fiscal note for **House File 306** as amended by **Amendment H-1202** 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.

House File 306 expands an existing apportionment benefit available to certain Subchapter S corporations. Under current law, Subchapter S corporations classified as "value-added" businesses may apportion income such that Iowa income tax is only levied on sales within the State of Iowa. Eligible corporations submit claims for refunds equal to the difference between their tax under apportionment and their tax without single-factor apportionment. Under current law, after receiving all claims for refunds, the Department of Revenue and Finance prorates claims such that total aggregate claims do not exceed \$5.0 million.

The Bill repeals the requirement that a corporation be a "value-added" corporation, and also removes the standing limited cap of \$5.0 million.

All Subchapter S corporations will be eligible for the single-factor apportionment election effective January 1, 1998. The \$5.0 million aggregate limitation is repealed retroactive to January 1, 1997.

Amendment H-1202 expands the provisions to partnerships, sole proprietorships, and limited liability companies. The number of partnerships and LLCs is growing, but most would not elect a change in tax status. There are an estimated 200,000 sole proprietorships in Iowa, but it is not known the extent to which these small businesses do business within and without the State. It is unlikely that more than several thousand sole proprietors would be qualify for the provisions of the Bill.

FISCAL IMPACT

House File 306 is expected to result in a decrease in revenues to the General Fund of approximately \$5.0 million in FY 1998 and \$3.0 million in FY 1999. The total cost of single-factor apportionment for Subchapter S corporations is estimated to be \$8.0 million annually. Of this amount, \$5.0 million already exists under current law.

Amendment H-1202 is expected to result in an additional decrease in revenues to the General Fund of an amount less than \$3.0 million in FY 1999 and subsequent fiscal years. The actual cost will be less to the extent that sole proprietorships, partnerships, and LLCs can elect to become Subchapter S corporations in the absence of the Amendment

SOURCES

Department of Revenue and Finance

Legislative Tax Model
Secretary of State

(LSB 1372hv.4, JAM)

**HOUSE FILE 306
FISCAL NOTE**

A fiscal note for House File 306 as amended by Amendment H-1180 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.

House File 306 expands an existing apportionment benefit available to certain Subchapter S corporations. Under current law, Subchapter S corporations classified as "value-added" businesses may apportion income such that Iowa income tax is only levied on sales within the State of Iowa. Eligible corporations submit claims for refunds equal to the difference between their tax under apportionment and their tax without single-factor apportionment. Under current law, after receiving all claims for refunds, the Department of Revenue and Finance prorates claims such that total aggregate claims do not exceed \$5.0 million.

The Bill repeals the requirement that a corporation be a "value-added" corporation, and also removes the standing limited cap of \$5.0 million.

All Subchapter S corporations will be eligible for the single-factor apportionment election effective January 1, 1998. The \$5.0 million aggregate limitation is repealed retroactive to January 1, 1997.

Amendment H-1180 expands the apportionment benefits to limited liability companies (LLCs) doing business within and without the State. Although the number of LLCs registered in Iowa is growing, most of them would not be classified as doing business within and without the State, and would probably not choose to elect to be taxed as C corporations. This fiscal note assumes that more than 75.0% of LLCs would be unaffected by the Bill.

FISCAL IMPACT

House File 306 is expected to result in a decrease in revenues to the General Fund of approximately \$5.0 million in FY 1998 and \$3.0 million in FY 1999. The total cost of single-factor apportionment for Subchapter S corporations is estimated to be \$8.0 million annually. Of this amount, \$5.0 million already exists under current law.

Amendment H-1180 is expected to result in an additional decrease in revenues to the General Fund of an amount less than \$2.0 million in FY 1999 and subsequent fiscal years. The actual loss would be less to the extent that most LLCs could elect to become Subchapter S corporations in the absence of this Amendment.

SOURCES

Department of Revenue and Finance
Secretary of State

(LSB 1372hv.3, JAM)

**HOUSE FILE 306
FISCAL NOTE**

A fiscal note for **House File 306** 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.

House File 306 expands an existing apportionment benefit available to certain Subchapter S corporations. Under current law, Subchapter S corporations classified as "value-added" businesses may apportion income such that Iowa income tax is only levied on sales within the State of Iowa. Eligible corporations submit claims for refunds equal to the difference between their tax under apportionment and their tax without single-factor apportionment. Under current law, after receiving all claims for refunds, the Department of Revenue and Finance prorates claims such that total aggregate claims do not exceed \$5.0 million.

The Bill repeals the requirement that a corporation be a "value-added" corporation, and also removes the standing limited cap of \$5.0 million.

All Subchapter S corporations will be eligible for the single-factor apportionment election effective January 1, 1998. The \$5.0 million aggregate limitation is repealed retroactive to January 1, 1997.

FISCAL IMPACT

House File 306 is expected to result in a decrease in revenues to the General Fund of approximately \$5.0 million in FY 1998 and \$3.0 million in FY 1999. The total cost of single-factor apportionment for Subchapter S corporations is estimated to be \$8.0 million annually. Of this amount, \$5.0 million already exists under current law.

SOURCES

Department of Revenue and Finance

(LSB 1372hv, JAM)

FILED FEBRUARY 24, 1997

BY DENNIS PROUTY, FISCAL DIRECTOR

**HOUSE FILE 306
FISCAL NOTE**

A fiscal note for House File 306 as amended by H-1128 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.

House File 306 expands an existing apportionment benefit available to certain Subchapter S corporations. Under current law, Subchapter S corporations classified as "value-added" businesses may apportion income such that Iowa income tax is only levied on sales within the State of Iowa. Eligible corporations submit claims for refunds equal to the difference between their tax under apportionment and their tax without single-factor apportionment. Under current law, after receiving all claims for refunds, the Department of Revenue and Finance prorates claims such that total aggregate claims do not exceed \$5.0 million.

The Bill repeals the requirement that a corporation be a "value-added" corporation, and also removes the standing limited cap of \$5.0 million.

All Subchapter S corporations will be eligible for the single-factor apportionment election effective January 1, 1998. The \$5.0 million aggregate limitation is repealed retroactive to January 1, 1997.

Amendment H-1128 expands the provisions to partnerships and sole proprietorships. In 1995 there were 159 Limited Liability Partnerships (LLPs) registered with the Secretary of State. There are an estimated 200,000 sole proprietorships in Iowa, but it is not known the extent to which these small businesses do business within and without the State. It is unlikely that more than several thousand sole proprietors would be qualify for the provisions of the Bill.

FISCAL IMPACT

House File 306 is expected to result in a decrease in revenues to the General Fund of approximately \$5.0 million in FY 1998 and \$3.0 million in FY 1999. The total cost of single-factor apportionment for Subchapter S corporations is estimated to be \$8.0 million annually. Of this amount, \$5.0 million already exists under current law.

Amendment H-1288 is expected to result in an additional decrease in revenues to the General Fund of an amount less than \$1.0 million in FY 1999 and subsequent fiscal years.

SOURCES

Department of Revenue and Finance
Legislative Tax Model

(LSB 1372hv.2, JAM)

HOUSE FILE 306

H-1180

1 Amend House File 306 as follows:

- 2 1. Page 1, line 12, by inserting after the word
3 "state" the following: "or resident member of a
4 limited liability company which carries on business
5 within and without the state".
- 6 2. Page 1, line 19, by inserting after the word
7 "shareholder" the following: "or member".
- 8 3. Page 1, line 22, by inserting after the word
9 "shareholder" the following: "or member".
- 10 4. Page 1, line 25, by inserting after the word
11 "shareholder" the following: "or member".
- 12 5. Page 3, line 24, by inserting after the word
13 "state," the following: "or resident member of a
14 limited liability company which carries on business
15 within and without the state,".
- 16 6. Page 4, line 13, by striking the words and
17 figure "unnumbered paragraph 1,".
- 18 7. Page 4, line 15, by inserting before the word
19 "A" the following: "b."
- 20 8. Page 4, line 18, by inserting after the word
21 "corporation" the following: "or limited liability
22 company".
- 23 9. Page 4, line 20, by inserting after the word
24 "shareholders" the following: "or members".
- 25 10. Page 4, by inserting after line 22 the
26 following:
27 "(1) The net income or loss of the corporation or
28 limited liability company which is fairly and
29 equitably attributable to this state under in the
30 manner provided in section 422.33, subsections 2 and
31 3.
- 32 (2) Any cash or the value of property
33 distributions which are made only to the extent that
34 they are paid from income upon which Iowa income tax
35 has not been paid, as determined under rules of the
36 director, reduced by fifty percent of the amount of
37 any of these distributions that are made to enable the
38 shareholder to pay federal income tax on items of
39 income, loss, and expenses from the corporation or
40 reduced by one hundred percent of such amount in the
41 case of a limited liability company."
- 42 11. Page 4, line 27, by inserting after the word
43 "Code," the following: "or is a member,".
- 44 12. Page 4, line 31, by inserting after the word
45 "Code" the following: "or limited liability company".
- 46 13. Title page, line 3, by inserting before the
47 word "and" the following: "and to members of limited
48 liability companies".

By GRUNDBERG of Polk
LARSON of Linn

H-1180 FILED MARCH 17, 1997

WITHDRAWN
3/18/97

H-1128

- 1 Amend House File 306 as follows:
- 2 1. Page 1, line 12, by inserting after the word
- 3 "state" the following: "or resident sole proprietor
- 4 or resident partner in a partnership which carries on
- 5 business within and without the state".
- 6 2. Page 1, line 19, by inserting after the word
- 7 "shareholder" the following: ", sole proprietor, or
- 8 partner".
- 9 3. Page 1, line 22, by inserting after the word
- 10 "shareholder" the following: ", sole proprietor, or
- 11 partner".
- 12 4. Page 1, line 25, by inserting after the word
- 13 "shareholder" the following: ", sole proprietor, or
- 14 partner".
- 15 5. Page 3, line 24, by inserting after the word
- 16 "state" the following: "resident sole proprietor or
- 17 resident partner in a partnership which carries on
- 18 business within and without the state".
- 19 6. Page 4, line 13, by striking the words and
- 20 figure "unnumbered paragraph 1,".
- 21 7. Page 4, line 15, by inserting before the word
- 22 "A" the following: "b."
- 23 8. Page 4, line 18, by inserting after the word
- 24 "corporation" the following: ", sole proprietorship,
- 25 or partnership".
- 26 9. Page 4, line 20, by inserting after the word
- 27 "shareholders" the following: ", sole proprietor, or
- 28 partners".
- 29 10. Page 4, by inserting after line 22 the
- 30 following:
- 31 "(1) The net income or loss of the corporation,
- 32 sole proprietorship, or partnership which is fairly
- 33 and equitably attributable to this state under in the
- 34 manner provided in section 422.33, subsections 2 and
- 35 3.
- 36 (2) Any cash or the value of property
- 37 distributions which are made only to the extent that
- 38 they are paid from income upon which Iowa income tax
- 39 has not been paid, as determined under rules of the
- 40 director, reduced by fifty percent of the amount of
- 41 any of these distributions that are made to enable the
- 42 shareholder to pay federal income tax on items of
- 43 income, loss, and expenses from the corporation or
- 44 reduced by one hundred percent of such amount in the
- 45 case of a sole proprietorship, or partnership."
- 46 11. Page 4, line 27, by inserting after the word
- 47 "Code," the following: "sole proprietor, or
- 48 partner,".
- 49 12. Page 4, line 31, by inserting after the word
- 50 "Code" the following: ", sole proprietorship, or

H-1128

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H-1128

Page 2

- 1 partnership".
- 2 13. Title page, line 3, by inserting before the
- 3 word "and" the following: ", to sole proprietors, and
- 4 partners of partnerships".

By RICHARDSON of Warren

H-1128 FILED FEBRUARY 27, 1997

WITHDRAWN

3/18/97 (p.668)

HOUSE FILE 306

H-1202

1 Amend House File 306 as follows:

2 1. Page 1, line 12, by inserting after the word
3 "state" the following: "or resident shareholder of a
4 professional corporation, resident sole proprietor,
5 resident partner in a partnership, or resident member
6 of a limited liability company which carries on
7 business within and without the state".

8 2. Page 1, line 19, by inserting after the word
9 "shareholder" the following: ", sole proprietor,
10 partner, or member".

11 3. Page 1, line 22, by inserting after the word
12 "shareholder" the following: ", sole proprietor,
13 partner, or member".

14 4. Page 1, line 25, by inserting after the word
15 "shareholder" the following: ", sole proprietor,
16 partner, or member".

17 5. Page 3, line 24, by inserting after the word
18 "state," the following: "resident shareholder of a
19 professional corporation, resident sole proprietor,
20 resident partner in a partnership, or resident member
21 of a limited liability company which carries on
22 business within and without the state,".

23 6. Page 4, line 13, by striking the words and
24 figure "unnumbered paragraph 1,".

25 7. Page 4, line 15, by inserting before the word
26 "A" the following: "b."

27 8. Page 4, line 18, by inserting after the word
28 "corporation" the following: ", professional
29 corporation, sole proprietorship, partnership, or
30 limited liability company".

31 9. Page 4, line 20, by inserting after the word
32 "shareholders" the following: ", sole proprietor,
33 partners, or members".

34 10. Page 4, by inserting after line 22 the
35 following:

36 "(1) The net income or loss of the corporation,
37 sole proprietorship, partnership, or limited liability
38 company which is fairly and equitably attributable to
39 this state under in the manner provided in section
40 422.33, subsections 2 and 3.

41 (2) Any cash or the value of property
42 distributions which are made only to the extent that
43 they are paid from income upon which Iowa income tax
44 has not been paid, as determined under rules of the
45 director, reduced by fifty percent of the amount of
46 any of these distributions that are made to enable the
47 shareholder to pay federal income tax on items of
48 income, loss, and expenses from the corporation or
49 reduced by one hundred percent of such amount in the
50 case of a professional corporation, sole

H-1202

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1 proprietorship, partnership, or limited liability
2 company."

3 11. Page 4, line 27, by inserting after the word
4 "Code," the following: "shareholder, sole proprietor,
5 partner, member,".

6 12. Page 4, line 31, by inserting after the word
7 "Code" the following: ", shareholder, sole
8 proprietorship, partnership, or limited liability
9 company".

10 13. Title page, line 3, by inserting before the
11 word "and" the following: ", to shareholders of
12 professional corporations, sole proprietors, partners
13 of partnerships, and members of limited liability
14 companies".

By RICHARDSON of Warren

H-1202 FILED MARCH 17, 1997

WITHDRAWN
3/18/97

Larson, Ch
Lamberti
Shoultz

HSB 112
WAYS AND MEANS

Succeeded By
FILE 306

SENATE/HOUSE FILE _____
BY (PROPOSED GOVERNOR'S BILL)

Passed Senate, Date _____ Passed House, Date _____
Vote: Ayes _____ Nays _____ Vote: Ayes _____ Nays _____
Approved _____

A BILL FOR

1 An Act relating to the individual income tax by extending the
2 special method of computation of tax for value-added S
3 corporation shareholders to all S corporation shareholders and
4 eliminating the refund limitation and providing an effective
5 and applicability date provision.

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

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1 Section 1. Section 422.4, subsection 18, Code 1997, is
2 amended by striking the subsection.

3 Sec. 2. Section 422.5, subsection 1, paragraph j,
4 subparagraph (2), Code 1997, is amended to read as follows:

5 (2) The tax imposed upon the taxable income of a resident
6 shareholder in ~~a value-added~~ an S corporation which has in
7 effect for the tax year an election under subchapter S of the
8 Internal Revenue Code and carries on business within and
9 without the state may be computed by reducing the amount
10 determined pursuant to paragraphs "a" through "i" by the
11 amounts of nonrefundable credits under this division and by
12 multiplying this resulting amount by a fraction of which the
13 resident's net income allocated to Iowa, as determined in
14 section 422.8, subsection 2, paragraph "b", is the numerator
15 and the resident's total net income computed under section
16 422.7 is the denominator. If a resident shareholder has
17 elected to take advantage of this subparagraph, and for the
18 next tax year elects not to take advantage of this
19 subparagraph, the resident shareholder shall not reelect to
20 take advantage of this subparagraph for the three tax years
21 immediately following the first tax year for which the
22 shareholder elected not to take advantage of this
23 subparagraph, unless the director consents to the reelection.
24 This ~~paragraph~~ subparagraph also applies to individuals who
25 are residents of Iowa for less than the entire tax year.

26 ~~(a)--In order for a resident shareholder in a value-added~~
27 ~~corporation which has in effect for the tax year an election~~
28 ~~under subchapter S of the Internal Revenue Code and carries on~~
29 ~~business within and without the state, to claim the benefits~~
30 ~~of apportionment of income of the value-added S corporation,~~
31 ~~the taxpayer must completely fill out the return, determine~~
32 ~~the taxpayer's income tax liability without the benefit of~~
33 ~~apportionment of the value-added corporation's income, and pay~~
34 ~~the amount of tax owed.--The taxpayer shall recompute the~~
35 ~~taxpayer's income tax liability, by applying the provisions of~~

1 ~~this subparagraph on a special return.--This special return~~
2 ~~shall be filed under rules of the director and constitutes a~~
3 ~~claim for refund of the difference between the amount of tax~~
4 ~~the taxpayer paid as determined without the provisions of this~~
5 ~~subparagraph and the amount of tax determined with the~~
6 ~~provisions of this subparagraph.~~

7 (b) This subparagraph shall not affect the amount of the
8 taxpayer's checkoff to the Iowa election campaign fund under
9 section 56.18, the checkoff for the fish and game fund in
10 section 456A.16, the credits from tax provided in sections
11 422.10, 422.11A, and 422.12 and the allocation of these
12 credits between spouses if the taxpayers filed separate
13 returns or separately on combined returns.

14 (c) ~~For any tax year, the aggregate amount of refund~~
15 ~~claims that shall be paid pursuant to this subparagraph shall~~
16 ~~not exceed five million dollars.--If, for a tax year, the~~
17 ~~aggregate amount of refund claims filed pursuant to this~~
18 ~~subparagraph exceeds five million dollars, each claim for~~
19 ~~refund shall be paid on a pro-rata basis so that the aggregate~~
20 ~~amount of refund claims does not exceed five million dollars.~~
21 ~~In the case where refund claims are not paid in full, the~~
22 ~~amount of the refund to which the taxpayer is entitled under~~
23 ~~this subparagraph is the pro-rata amount that was paid and the~~
24 ~~taxpayer is not entitled to a refund of the unpaid portion and~~
25 ~~is not entitled to carry that amount forward or backward to~~
26 ~~another tax year.--Taxpayers shall not use refunds as~~
27 ~~estimated payments for the succeeding tax year.--Taxpayers~~
28 ~~whose tax years begin on January 1 must file their refund~~
29 ~~claims by October 31 of the calendar year following the end of~~
30 ~~their tax year to be eligible for refunds.--Taxpayers whose~~
31 ~~tax years begin on a date other than January 1 must file their~~
32 ~~refund claims by the end of the tenth month following the end~~
33 ~~of their tax years to be eligible.--The department shall~~
34 ~~determine on February 1 of the second succeeding calendar year~~
35 ~~if the total amount of claims for refund exceeds five million~~

1 dollars-for-the-tax-year.--Notwithstanding-any-other
2 provision, interest shall not be due on any refund claims that
3 are paid by the last day of February of the second succeeding
4 calendar year.--If the claim is not payable on February 1 of
5 the second succeeding calendar year, because the taxpayer is a
6 fiscal year filer, then the amount of the claim allowed shall
7 be in the same ratio as the refund claims available on
8 February 1 of the second succeeding calendar year.--These
9 claims shall be funded by moneys appropriated for payment of
10 individual income tax refunds.

11 Sec. 3. Section 422.5, subsection 1, paragraph k,
12 unnumbered paragraph 4, Code 1997, is amended to read as
13 follows:

14 In the case of a resident, including a resident estate or
15 trust, the state's apportioned share of the state alternative
16 minimum tax is one hundred percent of the state alternative
17 minimum tax computed in this subsection. In the case of a
18 resident or part-year resident shareholder in a value-added an
19 S corporation which has in effect for the tax year an election
20 under subchapter S of the Internal Revenue Code and carries on
21 business within and without the state, a nonresident,
22 including a nonresident estate or trust, or an individual,
23 estate, or trust that is domiciled in the state for less than
24 the entire tax year, the state's apportioned share of the
25 state alternative minimum tax is the amount of tax computed
26 under this subsection, reduced by the applicable credits in
27 sections 422.10 through 422.12 and this result multiplied by a
28 fraction with a numerator of the sum of state net income
29 allocated to Iowa as determined in section 422.8, subsection
30 2, paragraph "a" or "b" as applicable, plus tax preference
31 items, adjustments, and losses under subparagraph (1)
32 attributable to Iowa and with a denominator of the sum of
33 total net income computed under section 422.7 plus all tax
34 preference items, adjustments, and losses under subparagraph
35 (1). In computing this fraction, those items excludable under

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

9 Sec. 4. Section 422.8, subsection 2, paragraph b,
10 unnumbered paragraph 1, Code 1997, is amended to read as
11 follows:

12 A resident's income allocable to Iowa is the income
13 determined under section 422.7 reduced by items of income and
14 expenses from ~~a subchapter an~~ S corporation ~~which is a value-~~
15 ~~added corporation~~ that carries on business within and without
16 the state when those items of income and expenses pass
17 directly to the shareholders under provisions of the Internal
18 Revenue Code. These items of income and expenses are
19 increased by the greater of the following:

20 Sec. 5. Section 422.8, subsection 6, Code 1997, is amended
21 to read as follows:

22 6. If the resident or part-year resident is a shareholder
23 of ~~a value-added~~ an S corporation which has in effect an
24 election under subchapter S of the Internal Revenue Code,
25 subsections 1 and 3 do not apply to any income taxes paid to
26 another state or foreign country on the income from the ~~value-~~
27 ~~added~~ corporation which has in effect an election under
28 subchapter S of the Internal Revenue Code.

29 Sec. 6. This Act is effective January 1, 1998, and applies
30 to tax years beginning on or after that date.

31

EXPLANATION

32 Present law allows shareholders of an S corporation which
33 is a value-added corporation to reduce its individual income
34 tax by use of a different method of computing the tax. The
35 difference between the regular method and the alternative

1 method constitutes a claim for refund of tax owed. However,
2 the aggregate amount of refunds shall not exceed \$5 million
3 per tax year.

4 This bill expands the opportunity for a reduction in tax to
5 shareholders of all S corporations regardless of whether they
6 are value-added corporations or not. The bill also eliminates
7 the limitation of \$5 million on the aggregate amount of claims
8 for refunds.

9 The bill also provides that if a taxpayer elects to take
10 advantage of the provision to reduce the taxpayer's tax and
11 later elects not to take advantage of the tax reduction
12 provisions, then the taxpayer cannot reelect to take advantage
13 of the tax reduction provisions for the next three tax years
14 unless permitted by the director of revenue and finance.

15 The bill takes effect January 1, 1998, and applies to tax
16 years beginning on or after that date.

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