

*Substituted for
HF 305 3-12-97
(P. 568)*

FILED FEB 12 1997

SENATE FILE 129
BY COMMITTEE ON WAYS AND MEANS

(SUCCESSOR TO SSB 65)

Passed Senate, Date 2/20/97
Vote: Ayes 47 Nays 0

Passed House, Date 3-12-97
Vote: Ayes 98 Nays 0

Approved March 9, 1997
*(P. 1468) Passed 4-25-97
Vote 46-0*

A BILL FOR

1 An Act updating the Iowa Code references to the Internal Revenue
2 Code and providing a retroactive applicability date and an
3 effective date.

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

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S.F. 129

1 Section 1. Section 15.335, unnumbered paragraph 1, Code
2 1997, is amended to read as follows:

3 An eligible business may claim a corporate tax credit for
4 increasing research activities in this state during the period
5 the eligible business is participating in the program. The
6 credit equals six and one-half percent of the state's
7 apportioned share of the qualifying expenditures for
8 increasing research activities. The state's apportioned share
9 of the qualifying expenditures for increasing research
10 activities is a percent equal to the ratio of qualified
11 research expenditures in this state to total qualified
12 research expenditures. The credit allowed in this section is
13 in addition to the credit authorized in section 422.33,
14 subsection 5. If the eligible business is a partnership,
15 subchapter S corporation, limited liability company, or estate
16 or trust electing to have the income taxed directly to the
17 individual, an individual may claim the tax credit allowed.
18 The amount claimed by the individual shall be based upon the
19 pro rata share of the individual's earnings of the
20 partnership, subchapter S corporation, limited liability
21 company, or estate or trust. For purposes of this section,
22 "qualifying expenditures for increasing research activities"
23 means the qualifying expenditures as defined for the federal
24 credit for increasing research activities which would be
25 allowable under section 41 of the Internal Revenue Code in
26 effect on January 1, ~~1994~~ 1997.

27 Sec. 2. Section 15A.9, subsection 8, unnumbered paragraph
28 2, Code 1997, is amended to read as follows:

29 For the purposes of this section, "qualifying expenditures
30 for increasing research activities" means the qualifying
31 expenditures as defined for the federal credit for increasing
32 research activities which would be allowable under section 41
33 of the Internal Revenue Code in effect on January 1, ~~1996~~
34 1997. The credit authorized in this subsection is in lieu of
35 the credit authorized in section 422.33, subsection 5.

1 Sec. 3. Section 422.3, subsection 4, Code 1997, is amended
2 to read as follows:

3 4. "Internal Revenue Code" means the Internal Revenue Code
4 of 1954, prior to the date of its redesignation as the
5 Internal Revenue Code of 1986 by the Tax Reform Act of 1986,
6 or means the Internal Revenue Code of 1986 as amended to and
7 including ~~March-20,-1996~~ January 1, 1997, whichever is
8 applicable.

9 Sec. 4. Section 422.7, subsection 8, Code 1997, is amended
10 to read as follows:

11 8. Subtract the amount of the jobs work opportunity tax
12 credit allowable for the tax year under section 51 of the
13 Internal Revenue Code to the extent that the credit increased
14 federal adjusted gross income.

15 Sec. 5. Section 422.10, unnumbered paragraph 1, Code 1997,
16 is amended to read as follows:

17 The taxes imposed under this division shall be reduced by a
18 state tax credit for increasing research activities in this
19 state. For individuals, the credit equals six and one-half
20 percent of the state's apportioned share of the qualifying
21 expenditures for increasing research activities. The state's
22 apportioned share of the qualifying expenditures for
23 increasing research activities is a percent equal to the ratio
24 of qualified research expenditures in this state to total
25 qualified research expenditures. For purposes of this
26 section, an individual may claim a research credit for
27 qualifying research expenditures incurred by a partnership,
28 subchapter S corporation, estate, or trust electing to have
29 the income taxed directly to the individual. The amount
30 claimed by the individual shall be based upon the pro rata
31 share of the individual's earnings of a partnership,
32 subchapter S corporation, estate, or trust. For purposes of
33 this section, "qualifying expenditures for increasing research
34 activities" means the qualifying expenditures as defined for
35 the federal credit for increasing research activities which

1 would be allowable under section 41 of the Internal Revenue
2 Code in effect on January 1, 1995 1997.

3 Sec. 6. Section 422.33, subsection 5, unnumbered paragraph
4 1, Code 1997, is amended to read as follows:

5 The taxes imposed under this division shall be reduced by a
6 state tax credit for increasing research activities in this
7 state equal to six and one-half percent of the state's
8 apportioned share of the qualifying expenditures for
9 increasing research activities. The state's apportioned share
10 of the qualifying expenditures for increasing research
11 activities is a percent equal to the ratio of qualified
12 research expenditures in this state to the total qualified
13 research expenditures. For purposes of this subsection,
14 "qualifying expenditures for increasing research activities"
15 means the qualifying expenditures as defined for the federal
16 credit for increasing research activities which would be
17 allowable under section 41 of the Internal Revenue Code in
18 effect on January 1, 1995 1997.

19 Sec. 7. Section 422.35, subsection 5, Code 1997, is
20 amended to read as follows:

21 5. Subtract the amount of the jobs work opportunity tax
22 credit allowable for the tax year under section 51 of the
23 Internal Revenue Code to the extent that the credit increased
24 federal taxable income.

25 Sec. 8. This Act applies retroactively to January 1, 1996,
26 for tax years beginning on or after that date.

27 Sec. 9. This Act, being deemed of immediate importance,
28 takes effect upon enactment.

29

EXPLANATION

30 This bill updates the references to the Internal Revenue
31 Code to make the federal income tax revisions enacted by
32 Congress in 1996 applicable for Iowa income tax purposes. The
33 bill reflects the change in nomenclature of the federal jobs
34 tax credit to work opportunity tax credit. The bill updates
35 the Iowa Code references to the state research activities

1 credit for individuals, corporations, and corporations in
2 quality jobs enterprise zones to include the 1996 changes to
3 the federal research activities credits. The research
4 activities credit offered under the new jobs and income Act is
5 also updated.

6 The bill takes effect immediately upon enactment and
7 applies retroactively to tax years beginning on or after
8 January 1, 1996.

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SENATE FILE 129
FISCAL NOTE

A fiscal note for Senate File 129 as amended by Amendment S-3122 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.

Senate File 129 updates the references to the Internal Revenue Code to make the federal income tax revisions enacted by congress in 1996 applicable for Iowa income tax purposes. The Bill is retroactive to January 1, 1997.

There were eight provisions enacted by the federal government that have been identified as likely to affect State revenues. The following is a list of the provisions, including the FY 1997 and FY 1998 fiscal impact, expressed as (FY 1997 impact, FY 1998 impact).

1. Spousal IRAs - Non-working spouses under prior law could contribute \$250 to an IRA. This provision increases the contribution limit to \$2,000. (\$-0.1 million, \$-0.4 million)
2. Taxable Punitive Damages - Under prior law, many damage recoveries were non-taxable. (\$0.1 million, \$0.1 million)
3. Subchapter S Corporation Limits - Raised maximum number of shareholders from 35 to 75. (Insignificant impact, through it may have fiscal implications on the maximum State exposure resulting from pending Subchapter S corporation legislation at the State level).
4. Employer Education Exclusion - Expired provision, allows \$5,250 exclusion for assistance provided through employer education plan. (\$-2.3 million, \$-0.3 million)
5. Medical Savings Accounts - Pilot project for limited number of small business and self-employed persons. (\$-0.3 million, \$-0.6 million)
6. Long-Term Care Insurance - Long-term health insurance becomes eligible medical expense, which has implications for Iowa's 100% health insurance deduction. (Insignificant impact)
7. Nursing Home Deduction - Custodial nursing home expenses allowed as deduction, subject to limitations. (Insignificant impact)
8. Small Business Expense Deduction - Increased expense deduction from \$17,500 to \$25,000 over seven years. (\$-0.2 million, \$-0.5 million)

Amendment S-3122 allows low-income homebuyers to deduct from State taxable income the full amount of mortgage interest paid. Under current law, low-income homebuyers who qualify for a federal tax credit for mortgage interest are allowed to deduct 75.0% of their interest from their federal

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taxable income. The remaining 25.0% is taken in the form of a credit. Since mortgage interest for Iowa income tax purposes equals the amount taken on the federal return, these taxpayers can only deduct 75.0% of their mortgage interest, but Iowa law does not provide a credit in lieu of the lower deduction.

Amendment S-3122 would allow eligible taxpayers to add back the 25.0% of interest lost on the federal return. There are less than 1,000 new homebuyers each year that would be eligible. The average home price is approximately \$60,000. First time homebuyers are assumed to remain in their first home for eight to ten years on average.

FISCAL IMPACT

Senate File 129 is expected to result in a decrease in revenues to the General Fund of approximately \$2.8 million in FY 1997, and approximately \$1.7 million in FY 1998.

Amendment S-3122 is expected to result in a decrease in revenues to the General Fund of approximately \$500,000 in FY 1998 and subsequent fiscal years.

Senate File 129 as amended by S-3122 is expected to result in a decrease in revenues to the General Fund of \$2.8 million in FY 1997, and \$2.2 million in FY 1998.

SOURCES

Federation of Tax Administrators
Iowa Finance Authority
Department of Revenue and Finance

(LSB 1113SV.5, JAM)

FILED MARCH 13, 1997

BY DENNIS PROUTY, FISCAL DIRECTOR

**SENATE FILE 129
FISCAL NOTE**

A fiscal note for Senate File 129 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.

Senate File 129 updates the references to the Internal Revenue Code to make the federal income tax revisions enacted by congress in 1996 applicable for Iowa income tax purposes. The Bill is retroactive to January 1, 1997.

There were eight provisions enacted by the federal government that have been identified as likely to affect State revenues. The following is a list of the provisions, including the FY 1997 and FY 1998 fiscal impact, expressed as (FY 1997 impact, FY 1998 impact).

1. Spousal IRAs - Non-working spouses under prior law could contribute \$250 to an IRA. This provision increases the contribution limit to \$2,000. (\$-0.1 million, \$-0.4 million)
2. Taxable Punitive Damages - Under prior law, many damage recoveries were non-taxable. (\$0.1 million, \$0.1 million)
3. Subchapter S Corporation Limits - Raised maximum number of shareholders from 35 to 75. (Insignificant impact, through it may have fiscal implications on the maximum State exposure resulting from pending Subchapter S corporation legislation at the State level).
4. Employer Education Exclusion - Expired provision, allows \$5,250 exclusion for assistance provided through employer education plan. (\$-2.3 million, \$-0.3 million)
5. Medical Savings Accounts - Pilot project for limited number of small business and self-employed persons. (\$-0.3 million, \$-0.6 million)
6. Long-Term Care Insurance - Long-term health insurance becomes eligible medical expense, which has implications for Iowa's 100% health insurance deduction. (Insignificant impact)
7. Nursing Home Deduction - Custodial nursing home expenses allowed as deduction, subject to limitations. (Insignificant impact)
8. Small Business Expense Deduction - Increased expense deduction from \$17,500 to \$25,000 over seven years. (\$-0.2 million, \$-0.5 million)

FISCAL IMPACT

Senate File 129 is expected to result in a decrease in revenues to the General Fund of approximately \$2.8 million in FY 1997, and approximately \$1.7 million in FY 1998.

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SOURCES

Federation of Tax Administrators

(LSB 1113SV.4, JAM)

FILED FEBRUARY 19, 1997

BY DENNIS PROUTY, FISCAL DIRECTOR

SENATE FILE 129
FISCAL NOTE

A fiscal note for Senate File 129 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.

Senate File 129 updates the references to the Internal Revenue Code to make the federal income tax revisions enacted by congress in 1996 applicable for Iowa income tax purposes. The Bill is retroactive to January 1, 1997.

There were eight provisions enacted by the federal government that have been identified as likely to affect State revenues. The following is a list of the provisions, including the FY 1997 and FY 1998 fiscal impact, expressed as (FY 1997 impact, FY 1998 impact).

1. Spousal IRAs - Non-working spouses under prior law could contribute \$250 to an IRA. This provision increases the contribution limit to \$2,000. (\$-0.1 million, \$-0.4 million)
2. Taxable Punitive Damages - Under prior law, many damage recoveries were non-taxable. (\$0.1 million, \$0.1 million)
3. Subchapter S Corporation Limits - Raised maximum number of shareholders from 35 to 75. (Insignificant impact, through it may have fiscal implications on the maximum State exposure resulting from pending Subchapter S corporation legislation at the State level).
4. Employer Education Exclusion - Expired provision, allows \$5,250 exclusion for assistance provided through employer education plan. (\$-2.3 million, \$-2.6 million)
5. Medical Savings Accounts - Pilot project for limited number of small business and self-employed persons. (\$-0.3 million, \$-0.6 million)
6. Long-Term Care Insurance - Long-term health insurance becomes eligible medical expense, which has implications for Iowa's 100% health insurance deduction. (Insignificant impact)
7. Nursing Home Deduction - Custodial nursing home expenses allowed as deduction, subject to limitations. (Insignificant impact)
8. Small Business Expense Deduction - Increased expense deduction from \$17,500 to \$25,000 over seven years. (\$-0.2 million, \$-0.5 million)

FISCAL IMPACT

Senate File 129 is expected to result in a decrease in revenues to the General Fund of approximately \$2.8 million in FY 1997, and approximately \$3.9 million in FY 1998. Because some of the provisions expire, the costs are expected to

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decrease in FY 1999 and FY 2000.

SOURCES

Federation of Tax Administrators

(LSB 1113SV.3, JAM)

FILED FEBRUARY 13, 1997

BY DENNIS PROUTY, FISCAL DIRECTOR

SENATE FILE 129

S-3737

1 Amend the House amendment, S-3122, to Senate File
2 129 as passed by the Senate as follows:
3 1. Page 1, by inserting after line 2, the
4 following:
5 "____". Page 2, by inserting before line 1 the
6 following:
7 "Sec. 101. Section 97A.8, subsection 1, paragraph
8 i, Code 1997, is amended to read as follows:
9 i. (1) Notwithstanding paragraph "g" or other
10 provisions of this chapter, beginning January 1, 1995,
11 for federal income tax purposes, and beginning January
12 1, 1998, for state income tax purposes, member
13 contributions required under paragraph "f" or "h"
14 which are picked up by the department shall be
15 considered employer contributions for federal and
16 state income tax purposes, and the department shall
17 pick up the member contributions to be made under
18 paragraph "f" or "h" by its employees. The department
19 shall pick up these contributions by reducing the
20 salary of each of its employees covered by this
21 chapter by the amount which each employee is required
22 to contribute under paragraph "f" or "h" and shall
23 certify the amount picked up in lieu of the member
24 contributions to the department of revenue and
25 finance. The department of revenue and finance shall
26 forward the amount of the contributions picked up to
27 the board of trustees for recording and deposit in the
28 pension accumulation fund.
29 (2) Member contributions picked up by the
30 department under subparagraph (1) shall be treated as
31 employer contributions for federal and state income
32 tax purposes only and for all other purposes of this
33 chapter ~~and the laws of this state~~ shall be treated as
34 employee contributions and deemed part of the
35 employee's earnable compensation or salary.
36 Sec. 201. Section 97B.11A, Code 1997, is amended
37 to read as follows:
38 97B.11A PICKUP OF EMPLOYEE CONTRIBUTIONS.
39 1. Notwithstanding section 97B.11 or other
40 provisions of this chapter, beginning January 1, 1995,
41 for federal income tax purposes, and beginning January
42 1, 1998, for state income tax purposes, member
43 contributions required under section 97B.11 which are
44 picked up by the employer shall be considered employer
45 contributions for federal and state income tax
46 purposes, and each employer shall pick up the member
47 contributions to be made under section 97B.11 by its
48 employees. Each employer shall pick up these
49 contributions by reducing the salary of each of its
50 employees covered by this chapter by the amount which

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1 each employee is required to contribute under section
2 97B.11 and shall pay the amount picked up in lieu of
3 the member contributions as provided in section
4 97B.14.

5 2. Member contributions picked up by each employer
6 under subsection 1 shall be treated as employer
7 contributions for federal and state income tax
8 purposes only and for all other purposes of this
9 chapter ~~and the laws of this state~~ shall be treated as
10 employee contributions and deemed part of the
11 employee's wages or salary.

12 Sec. 301. Section 294.10A, Code 1997, is amended
13 to read as follows:

14 294.10A PICKUP OF TEACHER ASSESSMENTS.

15 1. Notwithstanding section 294.9 or other
16 provisions of this chapter, for federal income tax
17 purposes beginning January 1 following the submission
18 by a board of trustees of an application to the
19 federal internal revenue service requesting
20 qualification of a plan in accordance with the
21 requirements of the Internal Revenue Code, as defined
22 in section 422.3, and for state income tax purposes
23 beginning January 1, 1998, or January 1 following an
24 application for qualification, whichever is later,
25 teacher assessments required under section 294.9 which
26 are picked up by an employing school district shall be
27 considered employer contributions for federal and
28 state income tax purposes, and each employing school
29 district establishing a pension and annuity retirement
30 system pursuant to this chapter shall pick up the
31 teacher assessments to be made under section 294.9 by
32 its employees commencing on the January-1-following-an
33 application-for-qualification applicable date under
34 this subsection. Each employing school district shall
35 pick up these teacher assessments by reducing the
36 salary of each of the teachers covered by this chapter
37 by the amount which each teacher is required to
38 contribute through assessments under section 294.9 and
39 shall pay to the board of trustees the amount picked
40 up in lieu of the teacher assessments for recording
41 and deposit in the fund.

42 2. Teacher assessments picked up by each employing
43 school district under subsection 1 shall be treated as
44 employer contributions for federal and state income
45 tax purposes only and for all other purposes of this
46 chapter ~~and the laws of this state~~ shall be treated as
47 teacher assessments and deemed part of the teacher's
48 wages or salary.

49 Sec. 401. Section 411.8, subsection 1, paragraph
50 i, Code 1997, is amended to read as follows:

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Page 3

1 i. (1) Notwithstanding paragraph "g" or other
 2 provisions of this chapter, beginning January 1, 1995,
 3 for federal income tax purposes, and beginning January
 4 1, 1998, for state income tax purposes, member
 5 contributions required under paragraph "f" or "h"
 6 which are picked up by the city shall be considered
 7 employer contributions for federal and state income
 8 tax purposes, and each city shall pick up the member
 9 contributions to be made under paragraph "f" or "h" by
 10 its employees. Each city shall pick up these
 11 contributions by reducing the salary of each of its
 12 employees covered by this chapter by the amount which
 13 each employee is required to contribute under
 14 paragraph "f" or "h" and shall pay the amount picked
 15 up in lieu of the member contributions to the board of
 16 trustees for recording and deposit in the fund.

17 (2) Member contributions picked up by each city
 18 under subparagraph (1) shall be treated as employer
 19 contributions for federal and state income tax
 20 purposes only and for all other purposes of this
 21 chapter and the laws of this state shall be treated as
 22 employee contributions and deemed part of the
 23 employee's earnable compensation or salary."

24 2. Page 2, by inserting after line 14 the
 25 following:

26 "Sec. 501. Section 422.7, subsections 29 through
 27 31, Code 1997, are amended by striking the
 28 subsections."

29 3. Page 3, by striking lines 25 through 28 and
 30 inserting the following:

31 "Sec. 601. EFFECTIVE AND APPLICABILITY DATES.
 32 Sections 101, 201, 301, 401, and 501 of this Act take
 33 effect January 1, 1998, and apply to tax years
 34 beginning on or after January 1, 1998. Sections 1, 2,
 35 3, 4, 5, 6, and 7, being deemed of immediate
 36 importance, take effect upon enactment and apply
 37 retroactively to January 1, 1996, for tax years
 38 beginning on or after that date.""

39 2. Page 1, by inserting after line 11 the
 40 following:

41 " . Title page, line 2, by inserting after the
 42 word "Code" the following: "modifying the taxation of
 43 contributions to public retirement systems, "."

44 5. By renumbering as necessary.

By JOHN P. KIBBIE

JOHNIE HAMMOND

PATRICK J. DELUHERY

MARY A. LUNDBY

MARY LOU FREEMAN

MIKE CONNOLLY

S-3737 FILED APRIL 23, 1997

o/orden
 4/24/97 (p. 1468)

SENATE FILE 129

S-3709

1 Amend Senate File 129 as follows:

2 1. Page 2, by inserting before line 1 the

3 following:

4 "Sec. 101. Section 97A.8, subsection 1, paragraph

5 i, Code 1997, is amended to read as follows:

6 i. (1) Notwithstanding paragraph "g" or other

7 provisions of this chapter, beginning January 1, 1995,

8 for federal income tax purposes, and beginning January

9 1, 1998, for state income tax purposes, member

10 contributions required under paragraph "f" or "h"

11 which are picked up by the department shall be

12 considered employer contributions for federal and

13 state income tax purposes, and the department shall

14 pick up the member contributions to be made under

15 paragraph "f" or "h" by its employees. The department

16 shall pick up these contributions by reducing the

17 salary of each of its employees covered by this

18 chapter by the amount which each employee is required

19 to contribute under paragraph "f" or "h" and shall

20 certify the amount picked up in lieu of the member

21 contributions to the department of revenue and

22 finance. The department of revenue and finance shall

23 forward the amount of the contributions picked up to

24 the board of trustees for recording and deposit in the

25 pension accumulation fund.

26 (2) Member contributions picked up by the

27 department under subparagraph (1) shall be treated as

28 employer contributions for federal and state income

29 tax purposes only and for all other purposes of this

30 chapter and the laws of this state shall be treated as

31 employee contributions and deemed part of the

32 employee's earnable compensation or salary.

33 Sec. 201. Section 97B.11A, Code 1997, is amended

34 to read as follows:

35 97B.11A PICKUP OF EMPLOYEE CONTRIBUTIONS.

36 1. Notwithstanding section 97B.11 or other

37 provisions of this chapter, beginning January 1, 1995,

38 for federal income tax purposes, and beginning January

39 1, 1998, for state income tax purposes, member

40 contributions required under section 97B.11 which are

41 picked up by the employer shall be considered employer

42 contributions for federal and state income tax

43 purposes, and each employer shall pick up the member

44 contributions to be made under section 97B.11 by its

45 employees. Each employer shall pick up these

46 contributions by reducing the salary of each of its

47 employees covered by this chapter by the amount which

48 each employee is required to contribute under section

49 97B.11 and shall pay the amount picked up in lieu of

50 the member contributions as provided in section

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Page 2

1 97B.14.

2 2. Member contributions picked up by each employer
3 under subsection 1 shall be treated as employer
4 contributions for federal and state income tax
5 purposes only and for all other purposes of this
6 chapter ~~and the laws of this state~~ shall be treated as
7 employee contributions and deemed part of the
8 employee's wages or salary.

9 Sec. 301. Section 294.10A, Code 1997, is amended
10 to read as follows:

11 294.10A PICKUP OF TEACHER ASSESSMENTS.

12 1. Notwithstanding section 294.9 or other
13 provisions of this chapter, for federal income tax
14 purposes beginning January 1 following the submission
15 by a board of trustees of an application to the
16 federal internal revenue service requesting
17 qualification of a plan in accordance with the
18 requirements of the Internal Revenue Code, as defined
19 in section 422.3, and for state income tax purposes
20 beginning January 1, 1998, or January 1 following an
21 application for qualification, whichever is later,
22 teacher assessments required under section 294.9 which
23 are picked up by an employing school district shall be
24 considered employer contributions for federal and
25 state income tax purposes, and each employing school
26 district establishing a pension and annuity retirement
27 system pursuant to this chapter shall pick up the
28 teacher assessments to be made under section 294.9 by
29 its employees commencing on the ~~January 1 following an~~
30 application for qualification applicable date under
31 this subsection. Each employing school district shall
32 pick up these teacher assessments by reducing the
33 salary of each of the teachers covered by this chapter
34 by the amount which each teacher is required to
35 contribute through assessments under section 294.9 and
36 shall pay to the board of trustees the amount picked
37 up in lieu of the teacher assessments for recording
38 and deposit in the fund.

39 2. Teacher assessments picked up by each employing
40 school district under subsection 1 shall be treated as
41 employer contributions for federal and state income
42 tax purposes only and for all other purposes of this
43 chapter ~~and the laws of this state~~ shall be treated as
44 teacher assessments and deemed part of the teacher's
45 wages or salary.

46 Sec. 401. Section 411.8, subsection 1, paragraph
47 i, Code 1997, is amended to read as follows:

48 i. (1) Notwithstanding paragraph "g" or other
49 provisions of this chapter, beginning January 1, 1995,
50 for federal income tax purposes, and beginning January

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Page 3

1 1, 1998, for state income tax purposes, member
 2 contributions required under paragraph "f" or "h"
 3 which are picked up by the city shall be considered
 4 employer contributions for federal and state income
 5 tax purposes, and each city shall pick up the member
 6 contributions to be made under paragraph "f" or "h" by
 7 its employees. Each city shall pick up these
 8 contributions by reducing the salary of each of its
 9 employees covered by this chapter by the amount which
 10 each employee is required to contribute under
 11 paragraph "f" or "h" and shall pay the amount picked
 12 up in lieu of the member contributions to the board of
 13 trustees for recording and deposit in the fund.

14 (2) Member contributions picked up by each city
 15 under subparagraph (1) shall be treated as employer
 16 contributions for federal and state income tax
 17 purposes only and for all other purposes of this
 18 chapter ~~and the laws of this state~~ shall be treated as
 19 employee contributions and deemed part of the
 20 employee's earnable compensation or salary."

21 2. Page 2, by inserting after line 14 the
 22 following:

23 "Sec. 501. Section 422.7, subsections 29 through
 24 31, Code 1997, are amended by striking the
 25 subsections."

26 3. Page 3, by striking lines 25 through 28 and
 27 inserting the following:

28 "Sec. 601. EFFECTIVE AND APPLICABILITY DATES.
 29 Sections 101, 201, 301, 401, and 501 of this Act take
 30 effect January 1, 1998, and apply to tax years
 31 beginning on or after January 1, 1998. Sections 1, 2,
 32 3, 4, 5, 6, and 7, being deemed of immediate
 33 importance, take effect upon enactment and apply
 34 retroactively to January 1, 1996, for tax years
 35 beginning on or after that date."

36 4. Title page, line 2, by inserting after the
 37 word "Code" the following: "modifying the taxation of
 38 contributions to public retirement systems,".

39 5. By renumbering as necessary.

BY JOHN P. KIBBIE
 JOHNIE HAMMOND
 PATRICK J. DELUHERY

MARY A. LUNDBY
 MARY LOU FREEMAN
 MIKE CONNOLLY

S-3709 FILED APRIL 23, 1997

O/er der
4/24/97 (p. 1468)

SENATE FILE 129

H-1147

1 Amend Senate File 129, as passed by the Senate, as
2 follows:

3 1. Page 2, by inserting after line 14 the
4 following:

5 "Sec. ____ Section 422.9, subsection 2, Code 1997,
6 is amended by adding the following new paragraph:
7 NEW PARAGRAPH. f. Add the amount of the mortgage
8 interest credit allowable for the tax year under
9 section 25 of the Internal Revenue Code to the extent
10 the credit decreased the amount of interest deductible
11 under section 163(g) of the Internal Revenue Code."

By HUSER of Polk

H-1147 FILED MARCH 6, 1997

Adopted 3-12-97
(p. 56A)

SENATE FILE 129

S-3122

1 Amend Senate File 129, as passed by the Senate, as
2 follows:

3 1. Page 2, by inserting after line 14 the
4 following:

5 "Sec. ____ Section 422.9, subsection 2, Code 1997,
6 is amended by adding the following new paragraph:
7 NEW PARAGRAPH. f. Add the amount of the mortgage
8 interest credit allowable for the tax year under
9 section 25 of the Internal Revenue Code to the extent
10 the credit decreased the amount of interest deductible
11 under section 163(g) of the Internal Revenue Code."

Senate Document RECEIVED FROM THE HOUSE

S-3122 FILED MARCH 12, 1997

Ms Kibben, Chair
Redfern
Connolly

SSB 65
Ways & Means
Succeeded By
SF/HF 129

SENATE/HOUSE FILE
BY (PROPOSED DEPARTMENT OF
REVENUE AND FINANCE BILL)

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

A BILL FOR

1 An Act updating the Iowa Code references to the Internal Revenue
2 Code and providing a retroactive applicability date and an
3 effective date.

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

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1 Section 1. Section 15A.9, subsection 8, unnumbered
2 paragraph 2, Code 1997, is amended to read as follows:

3 For the purposes of this section, "qualifying expenditures
4 for increasing research activities" means the qualifying
5 expenditures as defined for the federal credit for increasing
6 research activities which would be allowable under section 41
7 of the Internal Revenue Code in effect on January 1, ~~1996~~
8 1997. The credit authorized in this subsection is in lieu of
9 the credit authorized in section 422.33, subsection 5.

10 Sec. 2. Section 422.3, subsection 4, Code 1997, is amended
11 to read as follows:

12 4. "Internal Revenue Code" means the Internal Revenue Code
13 of 1954, prior to the date of its redesignation as the
14 Internal Revenue Code of 1986 by the Tax Reform Act of 1986,
15 or means the Internal Revenue Code of 1986 as amended to and
16 including ~~March-20, 1996~~ January 1, 1997, whichever is
17 applicable.

18 Sec. 3. Section 422.7, subsection 8, Code 1997, is amended
19 to read as follows:

20 8. Subtract the amount of the jobs work opportunity tax
21 credit allowable for the tax year under section 51 of the
22 Internal Revenue Code to the extent that the credit increased
23 federal adjusted gross income.

24 Sec. 4. Section 422.10, unnumbered paragraph 1, Code 1997,
25 is amended to read as follows:

26 The taxes imposed under this division shall be reduced by a
27 state tax credit for increasing research activities in this
28 state. For individuals, the credit equals six and one-half
29 percent of the state's apportioned share of the qualifying
30 expenditures for increasing research activities. The state's
31 apportioned share of the qualifying expenditures for
32 increasing research activities is a percent equal to the ratio
33 of qualified research expenditures in this state to total
34 qualified research expenditures. For purposes of this
35 section, an individual may claim a research credit for

1 qualifying research expenditures incurred by a partnership,
2 subchapter S corporation, estate, or trust electing to have
3 the income taxed directly to the individual. The amount
4 claimed by the individual shall be based upon the pro rata
5 share of the individual's earnings of a partnership,
6 subchapter S corporation, estate, or trust. For purposes of
7 this section, "qualifying expenditures for increasing research
8 activities" means the qualifying expenditures as defined for
9 the federal credit for increasing research activities which
10 would be allowable under section 41 of the Internal Revenue
11 Code in effect on January 1, ~~1995~~ 1997.

12 Sec. 5. Section 422.33, subsection 5, unnumbered paragraph
13 1, Code 1997, is amended to read as follows:

14 The taxes imposed under this division shall be reduced by a
15 state tax credit for increasing research activities in this
16 state equal to six and one-half percent of the state's
17 apportioned share of the qualifying expenditures for
18 increasing research activities. The state's apportioned share
19 of the qualifying expenditures for increasing research
20 activities is a percent equal to the ratio of qualified
21 research expenditures in this state to the total qualified
22 research expenditures. For purposes of this subsection,
23 "qualifying expenditures for increasing research activities"
24 means the qualifying expenditures as defined for the federal
25 credit for increasing research activities which would be
26 allowable under section 41 of the Internal Revenue Code in
27 effect on January 1, ~~1995~~ 1997.

28 Sec. 6. Section 422.35, subsection 5, Code 1997, is
29 amended to read as follows:

30 5. Subtract the amount of the jobs work opportunity tax
31 credit allowable for the tax year under section 51 of the
32 Internal Revenue Code to the extent that the credit increased
33 federal taxable income.

34 Sec. 7. This Act applies retroactively to January 1, 1996,
35 for tax years beginning on or after that date.

LSB1113DP

MEMORANDUM

TO: Members of the 1997 General Assembly

FROM: The Iowa Department of Revenue and Finance

DATE: December 4, 1996

RE: The Bill Relating to Updating the Iowa Code to Include the Federal Income Tax Changes Made in 1996 and Providing Effective and Retroactive Applicability Dates for the Provision.

This is the annual bill proposed by the Department to include into Iowa income tax law, the federal income tax changes enacted by Congress in 1996 after March 20, 1996. The bill updates the three statutes for the Iowa research activities credits to include revisions in the federal research activities credit which is a basis for the Iowa credits. The Iowa statute which defines the Internal Revenue Code for Iowa income tax is also updated so the all the 1996 federal changes which affect the computation of Iowa net income are adopted. The two Iowa statutes for the federal jobs tax credit are revised to reflect the fact that the jobs tax credit has been replaced by the work opportunity tax credit. The changes in the bill are made retroactive to January 1, 1996, for tax years beginning on or after that date. The Act is made effective upon enactment.

Three income tax bills were enacted by Congress in August of 1996 and were signed by the president. These bills are the Small Business Job Protection Act of 1996, the Health Insurance Portability and Accountability Act of 1996 and the Personal Responsibility and Work Opportunity Reconciliation Act of 1996. Most of the provisions in the three acts are applicable for tax years beginning after 1996. However, there are a few provisions that apply for 1996 and a few more provisions that are applicable retroactively prior to 1996. In the following paragraphs we summarize those major provisions from the three federal acts which will impact Iowa income tax. Some of these provisions will effect income tax revenues. We will note the effective dates of only those provisions which are applicable other than for tax periods beginning on or after January 1, 1997.

The Small Business Job Protection Act includes a number of provisions that extend expiring tax benefits, simplify provisions for setting up pension plans and assist small businesses. For small businesses the amount of annual capital investment which may be expensed under section 179 of the Internal Revenue Code is increased in seven steps from the current \$17,500 per year in 1996 to \$25,000 in 2003 and years after 2003. The Act includes a number of provisions which relate to qualifications for business entities to become S corporations and increases the maximum number of eligible shareholders in an S corporation from 35 to 75. One S corporation revision

allows banks to become S corporations under some conditions. This change may effect the Iowa Franchise tax, since S corporations' earnings are taxed to the shareholders and not the business entity or the bank. This issue is addressed in the Department's annual administration bill.

This Act includes a number of provisions which simplify setting up pension plans for some small businesses. Deductible contributions of up to \$2000 may be made to individual retirement accounts for each spouse, if the combined compensation of both spouses is equal to the contributed amount. Under 1996 law the maximum amount that could be contributed to an IRA for a non-working spouse was \$250. Damage recoveries for non-physical injuries or illness are taxable if received in tax years ending after August 20, 1996. Under prior law many damage recoveries were non-taxable. The \$7,500 limit on contributions to deferred compensation plans of state and local governments and tax exempt organizations is increased in \$500 increments on the basis of inflation.

The Act provides tax credits to taxpayers that adopt children. Note that current Iowa law provides an additional itemized deduction for adoption expenses to the extent the expenses exceed 3% of the taxpayer's federal adjusted gross income. Since Iowa does not have an adoption tax credit, this provision has no impact on the Iowa tax structure.

The new work opportunity tax credit mentioned previously is a scaled-down version of the targeted jobs credit. The new credit is effective for first-year wages paid to employees who begin work after September 30, 1996 and before October 1, 1997. The exclusion for up to \$5,250 per year of assistance provided through an employer's education plan, which expired after 1994, is retroactively reinstated for tax years beginning after 1994. This exclusion is set to expire for assistance for courses beginning after May 31, 1997. The federal research activities credit for 20% of increased research expenses which expired June 30, 1995 is revived, but only for expenses paid or incurred during the period from July 1, 1996 through May 31, 1997. Note that although the Iowa research activities credit is based on the criteria for the federal credit, the Iowa credit also applies in situations where the federal credit was not effective.

The Health Insurance Portability and Accountability Act of 1996 includes a number of provisions that will give taxpayers tax benefits for health-related expenses. Under the Act, self-employed taxpayers are allowed increased percentage deductions for health insurance premiums for themselves, their spouses and their dependents. The percentage of health insurance premiums allowed as a deduction increase from the current 30% in 1996 to 40% in 1997 with a final increase to 80% in 2006 and later tax years. Under the act, insurance premiums for long-term care such as nursing home care are treated as medical expenses for tax years after 1996. Thus, for 1997 federal returns, long-term health insurance premiums will be allowed as itemized deduction for medical expenses, subject to the federal limitations. These insurance premiums will be allowed for purposes of the Iowa health insurance deduction on 1997 Iowa returns. The Act also allows a deduction for custodial nursing home expenses, subject to federal limitations on 1997 Iowa and federal returns. Long-term care insurance benefits are tax-free subject to a \$175 per day cap.

Medical Saving Accounts are authorized starting in 1997 under a four-year test plan. These accounts are available only to employees covered under an employer sponsored high-deductible plan of a "small" employer. To qualify as a "high deductible plan" a health insurance policy must have a deductible of from \$1,500 to \$2,250 for single coverage and a deductible of between \$3,000 to \$4,500 for family coverage. A "small" employer is one that employed on average no more than 50 employees in either of the two preceding years. A qualified employee may deduct from income subject to tax for the year an amount equal to the aggregate amount, generally not to exceed compensation paid in cash during the tax year by the individual to a Medical Savings Account (MSA). In general, the amount of annual contribution to an account that may be deducted on the income tax return is limited to 65% of the deductible amount for individuals and 75% of the deductible amount for family coverage. Accumulated earnings in MSA accounts are not taxed. Withdrawals from the accounts which are used to pay medical expenses are not taxable. However, withdrawals from the accounts not used for medical expenses are taxable and are subject to an additional 15% tax on the federal return. If the IRC Update bill is passed, contributions to Medical Savings Accounts will be deducted on the Iowa return to the extent the contributions were deductible on the federal return. Withdrawals from the MSA accounts will be taxable on the Iowa return to the same extent as the withdrawals were taxable on the federal return. However, unwarranted withdrawals from the accounts will not be subject to an additional 15% tax on the Iowa return unless such tax is authorized by the Iowa General Assembly.

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 includes a number of provisions designed to promote child support recovery by the various states. This Act also has a number of provisions related to computation of the federal earned income credit which is the basis for the Iowa earned income credit of 6.5% of the federal credit. The earned income credit provisions are applicable for 1996 federal returns.



SENATE FILE 129

AN ACT

UPDATING THE IOWA CODE REFERENCES TO THE INTERNAL REVENUE CODE
AND PROVIDING A RETROACTIVE APPLICABILITY DATE AND AN EFFECTIVE DATE.

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

Section 1. Section 15.335, unnumbered paragraph 1, Code 1997, is amended to read as follows:

An eligible business may claim a corporate tax credit for increasing research activities in this state during the period the eligible business is participating in the program. The credit equals six and one-half percent of the state's apportioned share of the qualifying expenditures for increasing research activities. The state's apportioned share of the qualifying expenditures for increasing research activities is a percent equal to the ratio of qualified research expenditures in this state to total qualified research expenditures. The credit allowed in this section is in addition to the credit authorized in section 422.33, subsection 5. If the eligible business is a partnership, subchapter S corporation, limited liability company, or estate or trust electing to have the income taxed directly to the individual, an individual may claim the tax credit allowed. The amount claimed by the individual shall be based upon the pro rata share of the individual's earnings of the partnership, subchapter S corporation, limited liability company, or estate or trust. For purposes of this section, "qualifying expenditures for increasing research activities" means the qualifying expenditures as defined for the federal credit for increasing research activities which would be allowable under section 41 of the Internal Revenue Code in effect on January 1, ~~1994~~ 1997.

Sec. 2. Section 15A.9, subsection 8, unnumbered paragraph 2, Code 1997, is amended to read as follows:

For the purposes of this section, "qualifying expenditures for increasing research activities" means the qualifying expenditures as defined for the federal credit for increasing research activities which would be allowable under section 41 of the Internal Revenue Code in effect on January 1, ~~1996~~ 1997. The credit authorized in this subsection is in lieu of the credit authorized in section 422.33, subsection 5.

Sec. 3. Section 422.3, subsection 4, Code 1997, is amended to read as follows:

4. "Internal Revenue Code" means the Internal Revenue Code of 1954, prior to the date of its redesignation as the Internal Revenue Code of 1986 by the Tax Reform Act of 1986, or means the Internal Revenue Code of 1986 as amended to and including ~~March 20, 1996~~ January 1, 1997, whichever is applicable.

Sec. 4. Section 422.7, subsection 8, Code 1997, is amended to read as follows:

8. Subtract the amount of the jobs work opportunity tax credit allowable for the tax year under section 51 of the Internal Revenue Code to the extent that the credit increased federal adjusted gross income.

Sec. 5. Section 422.9, subsection 2, Code 1997, is amended by adding the following new paragraph:

NEW PARAGRAPH. f. Add the amount of the mortgage interest credit allowable for the tax year under section 25 of the Internal Revenue Code to the extent the credit decreased the amount of interest deductible under section 163(g) of the Internal Revenue Code.

Sec. 6. Section 422.10, unnumbered paragraph 1, Code 1997, is amended to read as follows:

The taxes imposed under this division shall be reduced by a state tax credit for increasing research activities in this state. For individuals, the credit equals six and one-half

percent of the state's apportioned share of the qualifying expenditures for increasing research activities. The state's apportioned share of the qualifying expenditures for increasing research activities is a percent equal to the ratio of qualified research expenditures in this state to total qualified research expenditures. For purposes of this section, an individual may claim a research credit for qualifying research expenditures incurred by a partnership, subchapter S corporation, estate, or trust electing to have the income taxed directly to the individual. The amount claimed by the individual shall be based upon the pro rata share of the individual's earnings of a partnership, subchapter S corporation, estate, or trust. For purposes of this section, "qualifying expenditures for increasing research activities" means the qualifying expenditures as defined for the federal credit for increasing research activities which would be allowable under section 41 of the Internal Revenue Code in effect on January 1, 1995 ~~1997~~.

Sec. 7. Section 422.33, subsection 5, unnumbered paragraph 1, Code 1997, is amended to read as follows:

The taxes imposed under this division shall be reduced by a state tax credit for increasing research activities in this state equal to six and one-half percent of the state's apportioned share of the qualifying expenditures for increasing research activities. The state's apportioned share of the qualifying expenditures for increasing research activities is a percent equal to the ratio of qualified research expenditures in this state to the total qualified research expenditures. For purposes of this subsection, "qualifying expenditures for increasing research activities" means the qualifying expenditures as defined for the federal credit for increasing research activities which would be allowable under section 41 of the Internal Revenue Code in effect on January 1, 1995 ~~1997~~.

Sec. 8. Section 422.35, subsection 5, Code 1997, is amended to read as follows:

5. Subtract the amount of the jobs work opportunity tax credit allowable for the tax year under section 51 of the Internal Revenue Code to the extent that the credit increased federal taxable income.

Sec. 9. This Act applies retroactively to January 1, 1996, for tax years beginning on or after that date.

Sec. 10. This Act, being deemed of immediate importance, takes effect upon enactment.

MARY E. KRAMER
President of the Senate

RON J. CORBETT
Speaker of the House

I hereby certify that this bill originated in the Senate and is known as Senate File 129, Seventy-seventh General Assembly.

Approved May 9, 1997

MARY PAT GUNDERSON
Secretary of the Senate

TERRY E. BRANSTAD
Governor