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WAYS AND MEANS

HOUSE FILE

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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 state individual income  
2 tax by reducing the number of adjustments to federal adjusted  
3 gross income in computing the net income, modifying filing  
4 status options, and providing a second-earner tax credit, and  
5 including an effective and applicability date provision.  
6 BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF IOWA:

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HF 21

1 Section 1. Section 422.5, subsection 1, paragraph j,  
2 subparagraph (2), unnumbered paragraph 2, Code 1999, is  
3 amended to read as follows:

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

11 Sec. 2. Section 422.5, subsection 1, paragraph k,  
12 unnumbered paragraph 4, Code 1999, 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 an S corporation  
19 which has in effect for the tax year an election under  
20 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. 3. Section 422.5, subsection 2, Code 1999, is amended  
10 to read as follows:

11 2. However, the tax shall not be imposed on a resident or  
12 nonresident whose net income, as defined in section 422.7, is  
13 thirteen thousand five hundred dollars or less in the case of  
14 married persons filing jointly ~~or-filing-separately-on-a~~  
15 ~~combined-return~~, unmarried heads of household, and surviving  
16 spouses or nine thousand dollars or less in the case of all  
17 other persons; but in the event that the payment of tax under  
18 this division would reduce the net income to less than  
19 thirteen thousand five hundred dollars or nine thousand  
20 dollars as applicable, then the tax shall be reduced to that  
21 amount which would result in allowing the taxpayer to retain a  
22 net income of thirteen thousand five hundred dollars or nine  
23 thousand dollars as applicable. The preceding sentence does  
24 not apply to estates or trusts. For the purpose of this  
25 subsection, the entire net income, including any part of the  
26 net income not allocated to Iowa, shall be taken into account.  
27 For purposes of this subsection, net income includes all  
28 amounts of pensions or other retirement income received from  
29 any source which is not taxable under this division as a  
30 result of the government pension exclusions in section 422.7,  
31 or any other state law. If the combined net income of a  
32 husband and wife exceeds thirteen thousand five hundred  
33 dollars, neither of them shall receive the benefit of this  
34 subsection, and it is immaterial whether they file a joint  
35 return or separate returns. However, if a husband and wife

1 file separate returns and have a combined net income of  
2 thirteen thousand five hundred dollars or less, neither spouse  
3 shall receive the benefit of this paragraph, if one spouse has  
4 a net operating loss and elects to carry back or carry forward  
5 the loss as provided in section 422.9, subsection 3. A person  
6 who is claimed as a dependent by another person as defined in  
7 section 422.12 shall not receive the benefit of this  
8 subsection if the person claiming the dependent has net income  
9 exceeding thirteen thousand five hundred dollars or nine  
10 thousand dollars as applicable or the person claiming the  
11 dependent and the person's spouse have combined net income  
12 exceeding thirteen thousand five hundred dollars or nine  
13 thousand dollars as applicable.

14 In addition, if the married persons', filing jointly or  
15 ~~filing-separately-on-a-combined-return~~, unmarried head of  
16 household's, or surviving spouse's net income exceeds thirteen  
17 thousand five hundred dollars, the regular tax imposed under  
18 this division shall be the lesser of the maximum state  
19 individual income tax rate times the portion of the net income  
20 in excess of thirteen thousand five hundred dollars or the  
21 regular tax liability computed without regard to this  
22 sentence. Taxpayers electing to file separately shall compute  
23 the alternate tax described in this paragraph using the total  
24 net income of the husband and wife. The alternate tax  
25 described in this paragraph does not apply if one spouse  
26 elects to carry back or carry forward the loss as provided in  
27 section 422.9, subsection 3.

28 Sec. 4. Section 422.7, subsections 1 through 34, Code  
29 1999, are amended by striking the subsections and inserting in  
30 lieu thereof the following:

31 1. Subtract interest and dividends from federal  
32 securities.

33 2. Add interest and dividends from foreign securities and  
34 from securities of state and other political subdivisions  
35 exempt from federal income tax under the Internal Revenue

1 Code.

2 | 3. Subtract, to the extent included, the amount of  
3 additional social security benefits taxable under the Internal  
4 Revenue Code for tax years beginning on or after January 1,  
5 1994. The amount of social security benefits taxable as  
6 provided in section 86 of the Internal Revenue Code, as  
7 amended up to and including January 1, 1993, continues to  
8 apply for state income tax purposes for tax years beginning on  
9 or after January 1, 1994. Married taxpayers, who file a joint  
10 federal income tax return and who elect to file separate  
11 returns for state income tax purposes, shall allocate between  
12 the spouses the amount of benefits subtracted from net income  
13 in the ratio of the social security benefits received by each  
14 spouse to the total of these benefits received by both  
15 spouses.

16 4. Add interest and dividends from regulated investment  
17 companies exempt from federal income tax under the Internal  
18 Revenue Code and subtract the loss on the sale or exchange of  
19 a share of a regulated investment company held for six months  
20 or less to the extent the loss was disallowed under section  
21 852(b)(4)(B) of the Internal Revenue Code.

22 5. Subtract the net capital gain from the following:

23 a. (1) Net capital gain from the sale of real property  
24 used in a business, in which the taxpayer materially  
25 participated for ten years, as defined in section 469(h) of  
26 the Internal Revenue Code, and which has been held for a  
27 minimum of ten years, or from the sale of a business, as  
28 defined in section 422.42, in which the taxpayer was employed  
29 or in which the taxpayer materially participated for ten  
30 years, as defined in section 469(h) of the Internal Revenue  
31 Code, and which has been held for a minimum of ten years. The  
32 sale of a business means the sale of all or substantially all  
33 of the tangible personal property or service of the business.

34 However, where the business is sold to individuals who are  
35 all lineal descendants of the taxpayer, the taxpayer does not

1 have to have materially participated in the business in order  
2 for the net capital gain from the sale to be excluded from  
3 taxation.

4 However, in lieu of the net capital gain deduction in this  
5 paragraph and paragraphs "b", "c", and "d", where the business  
6 is sold to individuals who are all lineal descendants of the  
7 taxpayer, the amount of capital gain from each capital asset  
8 may be subtracted in determining net income.

9 (2) For purposes of this paragraph, "lineal descendant"  
10 means children of the taxpayer, including legally adopted  
11 children and biological children, stepchildren, grandchildren,  
12 great-grandchildren, and any other lineal descendants of the  
13 taxpayer.

14 b. Net capital gain from the sale of cattle or horses held  
15 by the taxpayer for breeding, draft, dairy, or sporting  
16 purposes for a period of twenty-four months or more from the  
17 date of acquisition; but only if the taxpayer received more  
18 than one-half of the taxpayer's gross income from farming or  
19 ranching operations during the tax year.

20 c. Net capital gain from the sale of breeding livestock,  
21 other than cattle or horses, if the livestock is held by the  
22 taxpayer for a period of twelve months or more from the date  
23 of acquisition; but only if the taxpayer received more than  
24 one-half of the taxpayer's gross income from farming or  
25 ranching operations during the tax year.

26 d. Net capital gain from the sale of timber as defined in  
27 section 631(a) of the Internal Revenue Code.

28 However, to the extent otherwise allowed, the deduction  
29 provided in this subsection is not allowed for purposes of  
30 computation of a net operating loss in section 422.9,  
31 subsection 3, and in computing the income for the taxable year  
32 or years for which a net operating loss is deducted.

33 6. Subtract, to the extent not otherwise deducted in  
34 computing adjusted gross income, the amounts paid by the  
35 taxpayer for the purchase of health benefits coverage or

1 insurance for the taxpayer or taxpayer's spouse or dependent.  
2 7. For a person who is disabled, or is fifty-five years of  
3 age or older, or is the surviving spouse of an individual or a  
4 survivor having an insurable interest in an individual who  
5 would have qualified for the exemption under this subsection  
6 for the tax year, subtract, to the extent included, the total  
7 amount of a governmental or other pension or retirement pay,  
8 including, but not limited to, defined benefit or defined  
9 contribution plans, annuities, individual retirement accounts,  
10 plans maintained or contributed to by an employer, or  
11 maintained or contributed to by a self-employed person as an  
12 employer, and deferred compensation plans or any earnings  
13 attributable to the deferred compensation plans, up to a  
14 maximum of five thousand dollars for a person, other than a  
15 husband or wife, who files a separate state income tax return  
16 and up to a maximum of ten thousand dollars for a husband and  
17 wife who file a joint state income tax return. However, a  
18 surviving spouse who is not disabled or fifty-five years of  
19 age or older can only exclude the amount of pension or  
20 retirement pay received as a result of the death of the other  
21 spouse. A husband and wife filing separate state income tax  
22 returns are allowed a combined maximum exclusion under this  
23 subsection of up to ten thousand dollars. The ten thousand  
24 dollar exclusion shall be allocated to the husband or wife in  
25 the proportion that each spouse's respective pension and  
26 retirement pay received bears to total combined pension and  
27 retirement pay received.

28 | Sec. 5. Section 422.9, subsection 2, paragraph i, Code  
29 1999, is amended to read as follows:

30 | i. If the taxpayer has a deduction for medical care  
31 expenses under section 213 of the Internal Revenue Code, the  
32 taxpayer shall recompute for the purposes of this subsection  
33 the amount of the deduction under section 213 by excluding  
34 from medical care, as defined in section 213, the amount  
35 subtracted under section 422.7, subsection 32 6.

1 Sec. 6. Section 422.12, Code 1999, is amended by adding  
2 the following new subsection:

3 NEW SUBSECTION. 2A. If married taxpayers file jointly, a  
4 second-earner tax credit equal to two and sixty-five  
5 hundredths percent of the taxable income of the lesser earning  
6 spouse.

7 Sec. 7. Section 422.12B, subsection 2, Code 1999, is  
8 amended to read as follows:

9 2. Married taxpayers electing to file separate returns or  
10 ~~filing-separately-on-a-combined-return~~ may avail themselves of  
11 the earned income credit by allocating the earned income  
12 credit to each spouse in the proportion that each spouse's  
13 respective earned income bears to the total combined earned  
14 income. Taxpayers affected by the allocation provisions of  
15 section 422.8 shall be permitted a deduction for the credit  
16 only in the amount fairly and equitably allocable to Iowa  
17 under rules prescribed by the director.

18 Sec. 8. Section 422.12C, subsection 3, Code 1999, is  
19 amended to read as follows:

20 3. Married taxpayers who have filed joint federal returns  
21 electing to file separate returns or ~~to file separately-on-a~~  
22 ~~combined-return-form~~ must determine the child and dependent  
23 care credit under subsection 1 based upon their combined net  
24 income and allocate the total credit amount to each spouse in  
25 the proportion that each spouse's respective net income bears  
26 to the total combined net income. Nonresidents or part-year  
27 residents of Iowa must determine their Iowa child and  
28 dependent care credit in the ratio of their Iowa source net  
29 income to their all source net income. Nonresidents or part-  
30 year residents who are married and elect to file separate  
31 returns or ~~to file separately-on-a-combined-return-form~~ must  
32 allocate the Iowa child and dependent care credit between the  
33 spouses in the ratio of each spouse's Iowa source net income  
34 to the combined Iowa source net income of the taxpayers.

35 Sec. 9. Section 422.21, unnumbered paragraphs 2 and 7,

1 Code 1999, are amended to read as follows:

2 An individual in the armed forces of the United States  
3 serving in an area designated by the president of the United  
4 States or the United States Congress as a combat zone, or an  
5 individual serving in support of those forces, is allowed the  
6 same additional time period after leaving the combat zone, or  
7 after a period of continuous hospitalization, to file a state  
8 income tax return or perform other acts related to the  
9 department, as would constitute timely filing of the return or  
10 timely performance of other acts described in section 7508(a)  
11 of the Internal Revenue Code. For the purposes of this  
12 paragraph, "other acts related to the department" includes  
13 filing claims for refund for any tax administered by the  
14 department, making tax payments other than withholding  
15 payments, filing appeals on the tax matters, filing other tax  
16 returns, and performing other acts described in the  
17 department's rules. The additional time period allowed  
18 applies to the spouse of the individual described in this  
19 paragraph to the extent the spouse files jointly ~~or-separately~~  
20 ~~on-the-combined-return-form~~ with the individual or when the  
21 spouse is a party with the individual to any matter for which  
22 the additional time period is allowed. For the purposes of  
23 this paragraph, the Internal Revenue Code shall be interpreted  
24 to include the provisions of Pub. L. No. 102-2.

25 If married taxpayers file a joint return ~~or-file-separately~~  
26 ~~on-a-combined-return~~ in accordance with rules prescribed by  
27 the director, both spouses are jointly and severally liable  
28 for the total tax due on the return, except when one spouse is  
29 considered to be an innocent spouse under criteria established  
30 pursuant to section 6013(e) of the Internal Revenue Code.

31 Sec. 10. Section 541A.3, subsection 2, Code 1999, is  
32 amended by striking the subsection.

33 Sec. 11. This Act, being deemed of immediate importance,  
34 takes effect upon enactment and applies retroactively to  
35 January 1, 1999, for tax years beginning on or after that

1 date.

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EXPLANATION

3 Under present law, the computation of individuals' income  
 4 tax begins with federal adjusted gross income with  
 5 approximately 32 adjustments. This bill reduces that to seven  
 6 adjustments which are presently available. These include the  
 7 exclusion of interest from federal securities, certain capital  
 8 gains, health coverage premiums, and some pension benefits,  
 9 less social security benefits being taxed, the inclusion of  
 10 state, foreign, and local government interest not specifically  
 11 excluded elsewhere in the Code, and the inclusion of certain  
 12 interest and dividends from regulated investment companies.

13 The bill eliminates the ability for married taxpayers to  
 14 file separately on a combined return and provides in lieu  
 15 thereof a second-earner tax credit.

16 The bill takes effect upon enactment and applies  
 17 retroactively to January 1, 1999, for tax years beginning on  
 18 or after that date.

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