

Larson, Chair
Teig
Weigel

HSB 550

WAYS AND MEANS

SUB

50 2535

HOUSE FILE _____

BY (PROPOSED COMMITTEE ON
WAYS AND MEANS BILL BY
CHAIRPERSON VAN FOSSEN)

Passed House, Date _____ Passed Senate, Date _____

Vote: Ayes _____ Nays _____ Vote: Ayes _____ Nays _____

Approved _____

A BILL FOR

1 An Act relating to the allocation to Iowa of income earned by an
2 S corporation for purposes of the state individual income tax
3 and including a retroactive applicability date provision.

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

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1 Section 1. Section 422.8, subsection 2, paragraph b,
2 subparagraph (2), Code 1999, is amended to read as follows:

3 (2) Any cash or the value of property distributions which
4 are made only to the extent that they are paid from income
5 upon which Iowa income tax has not been paid, as determined
6 under rules of the director, reduced by ~~fifty-percent-of~~ the
7 amount of any of these distributions that are made to enable
8 the shareholder to pay federal income tax on items of income,
9 loss, and expenses from the corporation.

10 Sec. 2. This Act applies retroactively to January 1, 2000,
11 for tax years beginning on or after that date.

12 EXPLANATION

13 Under the state individual income tax, resident
14 shareholders of S corporations doing business within and
15 without the state are allowed to allocate income between Iowa
16 and other states in determining their state income tax. As
17 part of the allocation procedure, under present law 50 percent
18 of the amount of an S corporation distribution received by a
19 shareholder, which is used to pay federal income tax, are not
20 allocated to Iowa. The bill increases this percentage to 100
21 percent.

22 The bill applies retroactively to January 1, 2000, for tax
23 years beginning on or after that date.

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MAR 3 2000
WAYS & MEANS CALENDAR

HOUSE FILE 2535
BY COMMITTEE ON WAYS AND MEANS

(SUCCESSOR TO HSB 550)

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Vote: Ayes _____ Nays _____ Vote: Ayes _____ Nays _____
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23 years beginning on or after that date.

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HOUSE FILE 2535

H-8573

1 Amend House File 2535 as follows:

2 1. By striking everything after the enacting
3 clause and inserting the following:

4 "Section 1. NEW SECTION. 422.11D ASSISTIVE
5 DEVICE TAX CREDIT -- SMALL BUSINESS.

6 1. The taxes imposed under this division, less the
7 credits allowed under sections 422.12 and 422.12B,
8 shall be reduced by an assistive device tax credit. A
9 small business purchasing, renting, or modifying an
10 assistive device or making workplace modifications for
11 an individual with a disability who is employed or
12 will be employed by the small business is entitled to
13 receive this assistive device tax credit which is
14 equal to fifty percent of the first five thousand
15 dollars paid during the tax year for the purchase,
16 rental, or modification of the assistive device or for
17 making the workplace modifications. Any credit in
18 excess of the tax liability shall be refunded with
19 interest computed under section 422.25. In lieu of
20 claiming a refund, a taxpayer may elect to have the
21 overpayment shown on the taxpayer's final, completed
22 return credited to the tax liability for the following
23 tax year. If the small business elects to take the
24 assistive device tax credit, the small business shall
25 reduce the deduction for the costs of purchasing,
26 renting, or modifying an assistive device or making
27 workplace modifications by the amount of the credit.

28 2. An individual may claim an assistive device tax
29 credit allowed a partnership, limited liability
30 company, S corporation, estate, or trust electing to
31 have the income taxed directly to the individual. The
32 amount claimed by the individual shall be based upon
33 the pro rata share of the individual's earnings of the
34 partnership, limited liability company, S corporation,
35 estate, or trust.

36 3. For purposes of this section:

37 a. "Assistive device" means any item, piece of
38 equipment, or product system which is used to
39 increase, maintain, or improve the functional
40 capabilities of an individual with a disability in the
41 workplace or on the job. "Assistive device" does not
42 mean any medical device, surgical device, or organ
43 implanted or transplanted into or attached directly to
44 an individual. "Assistive device" does not include
45 any device for which a certificate of title is issued
46 by the state department of transportation, but does
47 include any item, piece of equipment, or product
48 system otherwise meeting the definition of "assistive
49 device" that is incorporated, attached, or included as
50 a modification in or to such a device issued a

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1 certificate of title.

2 b. "Disability" means the same as defined in
3 section 225C.46.

4 c. "Small business" means a business that either
5 had gross receipts for its preceding tax year of three
6 million dollars or less or employed not more than
7 fourteen full-time employees during its preceding tax
8 year.

9 d. "Workplace modifications" means physical
10 alterations to the work environment.

11 Sec. 2. Section 422.33, Code Supplement 1999, is
12 amended by adding the following new subsection:

13 NEW SUBSECTION. 9. The taxes imposed under this
14 division shall be reduced by an assistive device tax
15 credit. A small business purchasing, renting, or
16 modifying an assistive device or making workplace
17 modifications for purposes of an individual with a
18 disability who is employed or will be employed by the
19 small business is entitled to receive this assistive
20 device tax credit which is equal to fifty percent of
21 the first five thousand dollars paid during the tax
22 year for the purchase, rental, or modification of the
23 assistive device or for making the workplace
24 modifications. Any credit in excess of the tax
25 liability shall be refunded with interest computed
26 under section 422.25. In lieu of claiming a refund, a
27 taxpayer may elect to have the overpayment shown on
28 the taxpayer's final, completed return credited to the
29 tax liability for the following tax year. If the
30 small business elects to take the assistive device tax
31 credit, the small business shall reduce the deduction
32 for the costs of purchasing, renting, or modifying an
33 assistive device or making workplace modifications by
34 the amount of the credit.

35 a. For purposes of this subsection, "assistive
36 device" means any item, piece of equipment, or product
37 system which is used to increase, maintain, or improve
38 the functional capabilities of an individual with a
39 disability in the workplace or on the job. "Assistive
40 device" does not mean any medical device, surgical
41 device, or organ implanted or transplanted into or
42 attached directly to an individual. "Assistive
43 device" does not include any device for which a
44 certificate of title is issued by the state department
45 of transportation, but does include any item, piece of
46 equipment, or product system otherwise meeting the
47 definition of "assistive device" that is incorporated,
48 attached, or included as a modification in or to such
49 a device issued a certificate of title.

50 b. "Disability" means the same as defined in

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Page 3

1 section 225C.46.

2 c. "Small business" means a business that either
3 had gross receipts for its preceding tax year of three
4 million dollars or less or employed not more than
5 fourteen full-time employees during its preceding tax
6 year.

7 d. "Workplace modifications" means physical
8 alterations to the work environment.

9 Sec. 3. EFFECTIVE AND RETROACTIVE APPLICABILITY
10 DATE. This Act, being deemed of immediate importance,
11 takes effect upon enactment and applies retroactively
12 to January 1, 2000, for tax years beginning on or
13 after that date."

14 2. Title page, by striking lines 1 through 3 and
15 inserting the following: "An Act providing an
16 individual and corporate tax credit for the
17 acquisition or modification of assistive technology or
18 the modification of the workplace in order to assist
19 persons with a disability in the workplace and
20 including an effective and retroactive applicability
21 date provision."

By WEIGEL of Chickasaw

H-8573 FILED MARCH 28, 2000

HOUSE FILE 2535

H-8572

1 Amend House File 2535 as follows:

2 1. Page 1, line 7, by inserting after the word
3 "amount" the following: ", not to exceed one hundred
4 thousand dollars,".

By WEIGEL of Chickasaw

H-8572 FILED MARCH 28, 2000

HOUSE FILE 2535

H-8570

1 Amend House File 2535 as follows:
2 1. By striking everything after the enacting
3 clause and inserting the following:
4 "Section 1. Section 422.121, Code Supplement 1999,
5 is amended to read as follows:
6 422.121 APPROPRIATION -- LIMITATION.
7 ~~Beginning with~~ For the fiscal ~~year~~ years beginning
8 July 1, 1997, July 1, 1998, and July 1, 1999, there is
9 appropriated annually from the general fund of the
10 state two million dollars to refund the credits
11 allowed under this division. For fiscal years
12 beginning on or after July 1, 2000, there is
13 appropriated annually from the general fund of the
14 state two million seven hundred fifty thousand dollars
15 to refund the credits allowed under this division.
16 Notwithstanding section 422.120, for tax years
17 beginning on or after January 1, 1997, the livestock
18 production tax credit shall only be allowed for cow-
19 calf operations. In calculating the tax credit for
20 cow-calf operations for tax years beginning in the
21 1997 calendar year, mature beef cows bred or for
22 breeding, bred yearling heifers, and breeding bulls in
23 the operations' inventory on December 31 of the tax
24 year which were also in the operations on July 1 of
25 the tax year and stockers and feeders sold during the
26 tax year may be counted. In calculating the tax
27 credit for cow-calf operations for tax years beginning
28 on or after January 1, 1998, only those bred cows,
29 bred heifers, and breeding bulls in the operations'
30 inventory on December 31 of the tax year which were
31 also in the operations on July 1 of the tax year may
32 be counted."
33 2. Title page, by striking lines 1 through 3 and
34 inserting the following: "An Act relating to the
35 appropriation made for the livestock production tax
36 credit."

By WEIGEL of Chickasaw

H-8570 FILED MARCH 28, 2000

HOUSE FILE 2535

H-8571

1 Amend House File 2535 as follows:
2 1. Page 1, by striking line 10 and inserting the
3 following:
4 "Sec. 2. This Act takes effect January 1, 2001,".
5 2. Title page, line 3, by striking the words "a
6 retroactive" and inserting the following: "an
7 effective and".

By WEIGEL of Chickasaw

H-8571 FILED MARCH 28, 2000

HOUSE FILE 2535

H-8622

1 Amend House File 2535 as follows:

2 1. Page 1, by inserting before line 1 the
3 following:

4 "Section 1. Section 96.19, subsection 41, Code
5 1999, is amended by adding the following new
6 paragraph:

7 NEW PARAGRAPH. f. Any payment made or attributed
8 to a shareholder of an S corporation, as defined in
9 section 1361 of the Internal Revenue Code, which was
10 based on the income after deduction of expenses of the
11 corporation and allocated based on the shareholder's
12 interest or investment in the corporation, unless all
13 or a portion of the payment was improperly
14 characterized and in fact represented compensation for
15 personal services in an employment relationship as
16 determined under subsection 18, paragraph "a",
17 subparagraph (2), then that portion of the payment
18 shall be deemed to be wages and the corporation shall
19 pay the appropriate contribution based on the facts as
20 they existed at the time the initial payment was made
21 or attributed, plus interest as provided by section
22 96.14, subsection 1, but shall not be liable for any
23 penalty if the payment is made within thirty days of
24 the final determination by the department."

25 2. Title page, line 1, by striking the words "to
26 Iowa".

27 3. Title page, line 2, by inserting after the
28 word "purposes" the following: "of the state
29 unemployment compensation tax and".

By HEATON of Henry

H-8622 FILED MARCH 28, 2000

HOUSE FILE 2535

H-8625

1 Amend House File 2535 as follows:

2 1. By striking everything after the enacting
3 clause and inserting the following:

4 "Section 1. There is appropriated from the general
5 fund of the state to the state board of regents for
6 the fiscal year beginning July 1, 2000, and ending
7 June 30, 2001, the following amount, or so much
8 thereof as may be necessary, to be used for the
9 purpose designated:

10 To Iowa state university of science and technology,
11 cooperative extension service in agriculture and home
12 economics, to support the Iowa concern hotline in
13 providing stress counseling, information, and referral
14 to farm families facing financial distress:

15 \$ 500,000

16 Notwithstanding section 8.33, moneys appropriated
17 in this section which remain unobligated or unexpended
18 at the close of the fiscal year shall not revert but
19 shall remain available to be used for the purposes
20 designated in the succeeding fiscal year."

21 2. Title page, by striking lines 1 through 3 and
22 inserting the following: "An Act appropriating money
23 to support the Iowa concern hotline to assist farm
24 families facing financial distress."

By WEIGEL of Chickasaw

H-8625 FILED MARCH 28, 2000

HOUSE FILE 2535

H-8867

1 Amend House File 2535 as follows:

2 1. By striking everything after the enacting
3 clause and inserting the following:

4 "Section 1. There is appropriated from the general
5 fund of the state to the department of education for
6 the fiscal year beginning July 1, 2000, and ending
7 June 30, 2001, the following amounts, or so much
8 thereof as may be necessary, to be used for the
9 purposes designated:

10 1. For the enrich Iowa pilot program:

11 \$ 1,500,000

12 a. Funds allocated for purposes of the enrich Iowa
13 pilot program as provided in this subsection shall be
14 distributed by the division of libraries and
15 information services to eligible public libraries that
16 are in compliance with performance measures adopted by
17 rule by the commission of libraries. The funds
18 allocated as provided in this subsection shall not be
19 used for the costs of administration by the division.
20 The amount distributed to each eligible public library
21 shall be based upon the following:

22 (1) The level of compliance by the eligible public
23 library with the performance measures adopted by the
24 commission as provided in this paragraph.

25 (2) The number of people residing within an
26 eligible library's geographic service area for whom
27 the library provides services.

28 (3) The amount of other funding the eligible
29 public library received in the previous fiscal year
30 for providing services to rural residents and to
31 contracting communities.

32 b. Moneys received by a public library under this
33 subsection shall supplement, not supplant, any other
34 funding received by the library.

35 c. For purposes of this subsection, "eligible
36 public library" means a public library that meets all
37 of the following requirements:

38 (1) Submits to the division all of the following:

39 (a) The report provided for under section 256.51,
40 subsection 1, paragraph "h".

41 (b) An application and accreditation report, in a
42 format approved by the commission, that provides
43 evidence of the library's compliance with at least one
44 level of the standards established in accordance with
45 section 256.51, subsection 1, paragraph "k".

46 (c) Any other application or report the division
47 deems necessary for the implementation of the enrich
48 Iowa pilot program.

49 (2) Participates in the library resource and
50 information sharing programs established by the state

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Page 2

1 library.

2 (3) Is a public library established by city
3 ordinance or a county library as provided in chapter
4 336.

5 d. Each eligible public library shall maintain a
6 separate listing within its budget for payments
7 received and expenditures made pursuant to this
8 subsection, and shall annually submit this listing to
9 the division.

10 e. By January 15, 2001, the division shall submit
11 a program evaluation report to the general assembly
12 and the governor detailing the uses and the impacts of
13 funds allocated under this subsection. It is the
14 intent of the general assembly to address the
15 continuation of the enrich Iowa pilot program during
16 the 2001 legislative session.

17 f. A public library that receives funds in
18 accordance with this subsection shall have an internet
19 filtering program or internet filtering service in use
20 unless the library has only one computer designated
21 for public use and the library staff regularly
22 monitors the use of that computer. However, a public
23 library that monitors the use of a computer shall
24 submit an annual report describing the library's
25 monitoring efforts to the division.

26 2. For state aid for regional libraries:

27 \$ 1,687,000"

28 2. Title page, by striking lines 1 through 3 and
29 inserting the following: "An Act appropriating moneys
30 to the department of education for the enrich Iowa
31 pilot program and for regional libraries."

By WEIGEL of Chickasaw

H-8867 FILED APRIL 12, 2000

**HOUSE FILE 2535
FISCAL NOTE**

A fiscal note for House File 2535 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 2535 allows taxpayers who elect to allocate income from S-corporations between Iowa and other states to deduct 100% of federal income taxes paid in determining the share of the S-corporation income that is subject to Iowa income tax. Currently, only 50% of federal income taxes paid may be deducted in determining the amount of S-corporation income that is subject to Iowa income tax. The Bill applies retroactively to January 1, 2000.

BACKGROUND

The Department of Revenue and Finance conducted a study of tax year 1998 returns to estimate the amount of deduction taken for federal taxes paid on S-corporation income. The analysis was based on a sample of returns claiming "Other Iowa Credits" on line 54 of the 1998 Iowa Individual Income Tax Long Form IA 1040. Based on the sample, \$8.6 million of S-corporation apportionment credits were estimated to have been claimed. To obtain an estimate of the impact of increasing the deduction for federal income taxes from 50% to 100%, the amount of the credit was reestimated for the 1,121 returns in the sample. With the change in the deduction the reestimated credit amount increased to \$9.4 million.

ASSUMPTIONS

1. Tax year 1998 was a typical year relative to the number of taxpayers reporting income from S-corporations and electing to apportion income between Iowa and other states.
2. The share of other credits claimed accounted for by the S-corporation apportionment credit remains relatively constant from year-to-year at approximately 60%.
3. The distribution of S-corporation apportionment credits by amount of the claim and adjusted gross income bracket of the taxpayers remains relatively constant from year-to-year.
4. The change in the deduction for federal taxes paid is made retroactive to January 1, 2000.
5. For tax year 2000 all of the deduction change impact will be realized on the tax return filed in FY 2001.
6. For tax year 2001, 12.5% of the impact will be realized in estimate payments made in FY 2001, 37.5% will be realized in estimate payments made in FY 2002, and 50.0% will be realized on final returns filed in FY 2002.

FISCAL IMPACT

House File 2535 will result in a decrease in General Fund revenues equal to \$0.9 million in FY 2001 and \$0.8 million in FY 2002.

SOURCE

Iowa Department of Revenue and Finance

(LSB 5821hv, MAL)

FILED MARCH 20, 2000

BY DENNIS PROUTY, FISCAL DIRECTOR