

**Senate File 309 - Introduced**

SENATE FILE 309

BY SCHULTZ

**A BILL FOR**

1 An Act relating to the exclusion from the individual income  
2 tax of certain net capital gains from the sale of real  
3 property used in a business, and including effective date  
4 and retroactive applicability provisions.

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

1 Section 1. Section 422.7, subsection 21, paragraph a, Code  
2 2017, is amended by adding the following new subparagraph:  
3 NEW SUBPARAGRAPH. (3) (a) For purposes of determining  
4 the material participation of a taxpayer under this paragraph  
5 with regard to a partnership, subchapter S corporation, limited  
6 liability company, estate, or trust whose capital gain flows  
7 through to the owners or beneficiaries for federal income tax  
8 purposes, material participation shall be determined at the  
9 owner or beneficiary level according to the activities of each  
10 owner or beneficiary.

11 (b) Notwithstanding subparagraph division (a), and  
12 notwithstanding any contrary provision of section 469(h) of  
13 the Internal Revenue Code, or any other contrary provision of  
14 law, for purposes of determining the material participation of  
15 a taxpayer under this paragraph with regard to the sale of an  
16 estate's or trust's real property used in a business or rental  
17 arrangement, for any year in which the decedent of the estate  
18 or one or more settlors, executors, or trustees of the estate  
19 or trust, as applicable, is materially participating in the  
20 estate's or trust's business or, if the estate's or trust's  
21 real property is leased to another person, is materially  
22 participating in the lessee's business that uses the real  
23 property, all the beneficiaries or owners of the estate or  
24 trust shall also be treated as materially participating in  
25 that business for that year. The requirement in subparagraph  
26 (1) of this paragraph that material participation occur for a  
27 period of ten years may be satisfied for a beneficiary or owner  
28 of an estate or trust by any combination of years of material  
29 participation by any decedent, settlor, executor, or trustee of  
30 the estate or trust attributable to the beneficiary or owner  
31 under this subparagraph division (b), aggregated over the ten  
32 years preceding the sale.

33 Sec. 2. REFUNDS. Refunds of taxes, interest, or penalties  
34 that arise from claims resulting from the enactment of this  
35 Act, for capital gains earned from sales occurring between

1 January 1, 2007, and the effective date of this Act, shall  
2 be limited to ten thousand dollars in the aggregate and  
3 shall not be allowed unless refund claims are filed prior to  
4 October 1, 2017, notwithstanding any other provision of law to  
5 the contrary. If the amount of claims totals more than ten  
6 thousand dollars in the aggregate, the department of revenue  
7 shall prorate the ten thousand dollars among all claimants in  
8 relation to the amounts of the claimant's valid claims.

9 Sec. 3. EFFECTIVE UPON ENACTMENT. This Act, being deemed of  
10 immediate importance, takes effect upon enactment.

11 Sec. 4. RETROACTIVE APPLICABILITY. This Act applies  
12 retroactively to January 1, 2007, for tax years beginning on  
13 or after that date.

14 EXPLANATION

15 The inclusion of this explanation does not constitute agreement with  
16 the explanation's substance by the members of the general assembly.

17 Under current law, a taxpayer's net capital gain from the  
18 sale of a business, or from the sale of real property used in  
19 a business, is exempt from the individual income tax if the  
20 taxpayer held the real property or the business for a minimum  
21 of 10 years, and materially participated in the business for  
22 10 years. "Material participation" refers to the level of  
23 involvement a taxpayer has in the operations of a business, and  
24 whether or not any particular taxpayer materially participates  
25 in a business is determined under the Internal Revenue Code.

26 This bill requires that for purposes of determining material  
27 participation of a taxpayer for the capital gain tax exemption  
28 with regard to a partnership, S corporation, limited liability,  
29 estate, or trust whose capital gain flows through to the owners  
30 or beneficiaries for federal income tax purposes, material  
31 participation shall be determined at the owner or beneficiary  
32 level according to the activities of each owner or beneficiary.

33 The bill also provides an exception to this material  
34 participation requirement for the sale of real property used  
35 in a business which, under certain circumstances, attributes

1 the material participation of certain representatives of an  
2 estate or trust to the beneficiaries or owners of that estate  
3 or trust. For purposes of determining material participation  
4 of a taxpayer with regard to the sale of an estate's or trust's  
5 real property used in a business or rental arrangement, all the  
6 beneficiaries or owners of the estate or trust shall be treated  
7 as materially participating in a business for any year that  
8 the decedent or one or more settlors, executors, or trustees  
9 of the estate or trust is materially participating in the  
10 estate's or trust's business or, if the real property is leased  
11 to another person, is materially participating in the lessee's  
12 business that uses the real property. The bill also provides  
13 that the 10-year material participation requirement can be  
14 satisfied for a beneficiary or owner of an estate or trust by  
15 any combination of years of material participation attributable  
16 to the beneficiary or owner under the bill, aggregated over the  
17 10 years preceding the sale.

18 The bill limits refunds of tax, interest, or penalties  
19 arising from claims resulting from the enactment of the bill  
20 for capital gains earned from sales occurring between January  
21 1, 2007, and the effective date of the bill to \$10,000 in  
22 the aggregate, and requires such claims to be filed prior to  
23 October 1, 2017. If the aggregate amount of refund claims  
24 exceeds \$10,000, the department of revenue is required to  
25 prorate the \$10,000 among all claimants in relation to each  
26 claim amount.

27 The bill takes effect upon enactment and applies  
28 retroactively to January 1, 2007, for tax years beginning on  
29 or after that date.