February 22, 1963.
Passed on File.
Ways and Means 2/25
Passed Senate, Date......................

Vote: Ayes............ Nays............

Senate File 248
By HILL.

Passed House, Date......................

Vote: Ayes............ Nays............

Approved..

A BILL FOR

An Act relating to the formula by which income of corporations is to be apportioned between the state of Iowa and other states for purposes of the Iowa income tax on corporations.

Be It Enacted by the General Assembly of the State of Iowa:

Section 1. Section four hundred twenty-two point thirty-three (422.33), Code 1962, is hereby repealed and the following enacted in lieu thereof:

"A tax is hereby imposed upon each corporation organized under the laws of this state, and upon every foreign corporation engaged in income producing activities in this state, annually in an amount equivalent to three percent of the net income received by such corporation during the income year.

1. If the income producing activities of the corporation are carried on entirely within the state, the tax shall be imposed on the entire net income, but if such income producing activities are carried on partly within and partly without the state, the tax shall be imposed only on the portion of the net income reasonably attributable to the state, said net income attributable to the state to be determined as follows:

a. Interest, dividends, rents, and royalties (less stated expenses) received in connection with income producing activities in the state, shall be allocated to the state, and where received in connection with income producing activities outside the state shall be allocated outside the state.

b. Net income of the above class having been separately allocated and deducted as above provided, the remainder of the net income of the taxpayer shall be allocated and apportioned as follows:

Where income is derived from income producing activities other than the manufacture or sale of tangible personal property or compensation for performance of labor or personal services, such income shall be specifically allocated or equitably apportioned within and without the state under rules and regulations of the commission.

Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to income producing activities within the state shall be allocated to Iowa on the basis of the percentage computed by taking the arithmetical average of the following three percentages:

(1). The percentage which the sales made in Iowa is of total sales wherever made. Sales made in Iowa include sales made through, from, or by offices, agencies, branches, stores or personal solicitation of salesmen or representatives in Iowa, whether or not such salesmen or representatives are residents of Iowa.

(2). The percentage which the total tangible property, real, personal, and mixed, owned or used by the taxpayer in this state in connection with such income producing activities, is of the total tangible property, real, personal, or mixed, wherever located, owned, or used by the taxpayer in connection with such income producing activities; and

(3). The percentage which the taxpayer's total payrolls paid or incurred in this state or paid in respect to labor performed in this state in connection with such income producing activities is of the taxpayer's total payrolls paid or incurred in connection with such income producing activities.

(4). In computing the percentages under subparagraphs one (1), two (2) and three (3) above the valuation of transient property, such as motor vehicles, shall be apportioned in a manner to reflect the use of such property within and without the state of Iowa. The valuation of tangible property, other than inventories, shall be its depreciated tax cost for income tax purposes at the end of the tax year, except that if such valuation does not fairly reflect the total tangible property owned or used by the taxpayer in this state during such tax year, such valuation shall be the average valuation of such property so owned or used during the tax year to be determined on the basis of sound accounting practices. All inventories shall be valued at total book cost at the end of the tax year, except that if such book cost does not fairly reflect the total inventory owned or used by the taxpayer during the tax year, such valuation shall be the average valuation of such property so owned or used during the tax year to be determined on the basis of sound accounting practices. For corporations occupying rented properties or using leased equipment, such property shall be valued at eight (8) times the annual net rental payments. For purposes of this computation, payrolls shall include wages, salaries, commissions, bonuses, and all remuneration paid as compensation for employees' personal services and shall be considered payrolls paid or incurred in this state, or paid in respect to labor performed in this state, if the duties of the employee normally require said employee to spend one-half or more of his working time in Iowa, without regard to the legal residence of the employee.

For the purpose of this section, the word 'sale' shall include exchange, and the word 'manufacture' shall include the extraction and recovery of natural resources and all processes of fabricating and curing. The words 'tangible personal property' shall be taken to mean corporeal personal property, such as machinery, tools, implements, goods, wares, and merchandise, and shall not be taken to mean money deposits in banks, shares of stock, bonds, notes, credits, or evidence of an interest in property and evidence of debt.

2. If any taxpayer believes that the method of allocation and apportionment hereinbefore prescribed, as administered by the commission and applied to his income producing activities has operated or will so operate as to subject him to taxation on a greater portion of his net income than is reasonably attributable to income producing activities within the state, he shall be entitled to file with the commission a statement of his objections and of such alternative method of allocation and apportionment as he believes to be proper under the circumstances with such detail and proof and within such time as the commission may reasonably prescribe; and if the commission shall conclude that the method of allocation and apportionment theretofore employed is in fact inapplicable and inequitable it shall redetermine the taxable income by such other method of allocation and apportionment as seems best calculated to assign to the state for taxation the portion of the income reasonably attributable to income producing activities within

the state.

3. If it shall appear to the tax commission that any allocation percentage determined as hereinabove provided does not properly reflect the income producing activities of a taxpayer within the state, the tax commission shall be authorized in its discretion, in case of the corporation allocation percentage, to adjust it by (a) excluding one or more of the factors therein, (b) including one or more other factors, or (c) any other similar or different method calculated to effect a fair and proper allocation of income reasonably attributable to the state. Upon such action by the tax commission the taxpayer will be informed in writing of the method to be used to allocate and apportion the income attributable to the state."

Sec. 2. Section four hundred twenty-two point forty (422.40), Code 1962, is hereby amended by striking from lines five (5) and six (6) of subsection one (1) the words, "doing business in this state for profit" and by inserting in lieu thereof the words, "engaged in income producing activities in this state."

EXPLANATION OF SENATE FILE 248

ADOPTION OF THE THREE-FACTOR ALLOCATION FORMULA

It is proposed that the present method of allocation (using only the sales factor) be replaced by a three-factor formula using sales, property and payroll as elements of the formula. Net income attributable to Iowa would then be computed as follows:

1. The percentage of Iowa sales to total sales would be computed.
2. The percentage of real and personal property in Iowa to total property wherever located would be computed. In this computation rented property would be included and valued at eight times the annual rent.
3. The percentage of the payroll paid to Iowa employees to total payroll would be computed.
4. The average of these three percentages would then be computed. This average would be the percentage of total net income allocated to Iowa for taxation.

In cases where either the tax commission or taxpayer was able to demonstrate that the formula would not result in an allocation which fairly reflected the taxpayer's Iowa income, the tax commission would be authorized to require or permit the use of a different method to achieve a fair result.

Examples of How the Amendment Would Work:

The following examples show how the present law and the proposed amendment would operate for several fictitious example corporations, each having an income after federal taxes of $100,000.

Example 1: Retailer doing business exclusively in Iowa

Percent of sales in Iowa	100%
Percent property in Iowa	100%
Percent of payroll in Iowa	100%
Average	100%

Income allocated to Iowa—present law	$100,000
Tax under present law	$ 3,000
Income allocated by three-factor formula	$100,000
Tax using three-factor formula	$ 3,000
Example 2: Iowa manufacturer selling on nationwide market	
Percent of sales in Iowa	10%
Percent of employees in Iowa	90%
Percent of property in Iowa	95%
Average	65%
Income allocated to Iowa—present law	$ 10,000
Tax under present law	$ 300
Income allocated by three-factor formula	$ 65,000
Tax using three-factor formula	$ 1,950
Example 3: Iowa wholesaler selling in several state areas	
Percent of sales in Iowa	40%
Payroll in Iowa	100%
Property in Iowa	100%
Average	80%
Income allocated to Iowa—present law	$ 40,000
Tax under present law	$ 1,200
Income allocated by three-factor formula	$ 80,000
Tax using three-factor formula	$ 2,400
Example 4: Out-of-state wholesaler or manufacturer selling on the national market	
Percent of sales in Iowa	10%
Percent of employees in Iowa	2%
Percent of property in Iowa	0%
Average	4%
Income allocated to Iowa—present law	$ 10,000
Tax under present law	$ 300
Income allocated to Iowa—under this Act	$ 400
Tax using three-factor formula	$ 12